IMPORTANT NOTICE

You must read the following before continuing. The following applies to the prospectus (in preliminary or final form) following this page (the "**Prospectus**"), and you are therefore advised to read this carefully before reading, accessing or making any other use of the Prospectus. In accessing the Prospectus, you agree to be bound by the following terms and conditions, including any modifications to them any time you receive any information from us as a result of such access.

NOTHING IN THIS ELECTRONIC TRANSMISSION CONSTITUTES AN OFFER TO SELL OR A SOLICITATION OF AN OFFER TO BUY THE SECURITIES DESCRIBED IN THE PROSPECTUS IN ANY JURISDICTION WHERE IT IS UNLAWFUL TO DO SO.

THE SECURITIES HAVE NOT BEEN REGISTERED UNDER THE UNITED STATES SECURITIES ACT OF 1933, AS AMENDED (THE "**SECURITIES ACT**") OR THE SECURITIES LAWS OF ANY STATE OF THE UNITED STATES OR OTHER RELEVANT JURISDICTION AND THE SECURITIES MAY NOT BE OFFERED OR SOLD WITHIN THE UNITED STATES OR TO, OR FOR THE ACCOUNT OR BENEFIT OF, U.S. PERSONS (AS DEFINED IN REGULATION S UNDER THE SECURITIES ACT ("**REGULATION S**")), EXCEPT IN A TRANSACTION NOT SUBJECT TO THE REGISTRATION REQUIREMENTS OF THE SECURITIES ACT AND IN ACCORDANCE WITH APPLICABLE STATE OR LOCAL SECURITIES LAWS.

THE PROSPECTUS MAY NOT BE FORWARDED OR DISTRIBUTED TO ANY OTHER PERSON AND MAY NOT BE REPRODUCED IN ANY MANNER WHATSOEVER. ANY FORWARDING, DISTRIBUTION OR REPRODUCTION OF THE PROSPECTUS IN WHOLE OR IN PART IS UNAUTHORISED. FAILURE TO COMPLY WITH THIS DIRECTIVE MAY RESULT IN A VIOLATION OF THE SECURITIES ACT OR THE APPLICABLE LAWS OF OTHER JURISDICTIONS.

Confirmation of your Representation: You have been sent the attached Prospectus at your request and by accepting the e-mail and by accepting the Prospectus you shall be deemed to have represented to The Co-operative Bank p.l.c. (the "**Issuer**") and to HSBC Bank plc and UBS Limited (together being the "**Joint Lead Managers**" referred to in the Prospectus and senders of the attached), (i) that you are not (or, if you are acting for another person, such person is not) a U.S. person, (ii) that you are not (or, if you are acting on behalf of another person, such person is not) located in the United States of America, its territories or possessions, any State of the United States or the District of Columbia (where "possessions" include Puerto Rico, the U.S. Virgin Islands, Guam, American Samoa, Wake Island and the Northern Mariana Islands) and (iii) that you consent (and if you are acting on behalf of another person, such person consents) to this delivery by electronic transmission.

You are reminded that the Prospectus has been delivered to you on the basis that you are a person into whose possession the Prospectus may be lawfully delivered in accordance with the laws of the jurisdiction in which you are located and you may not, nor are you authorised to, deliver the Prospectus to any other person.

The Prospectus does not constitute, and may not be used in connection with, an offer or solicitation to subscribe for or purchase any Notes by any person in any jurisdiction where offers or solicitations are not permitted by law. The distribution of the Prospectus and the offer or sale of the Notes in certain jurisdictions is restricted by law. If a jurisdiction requires that the offering be made by a licensed broker or dealer and any Joint Lead Manager or any affiliate of a Joint Lead Manager is a licensed broker or dealer in that jurisdiction, the offering shall be deemed to be made by such Joint Lead Manager or such affiliate on behalf of the Issuer in such jurisdiction. The Prospectus may only be communicated to persons in the United Kingdom in circumstances where section 21(1) of the Financial Services and Markets Act 2000 (as amended) does not apply.

The Prospectus has been sent to you in electronic form. You are reminded that documents transmitted via this medium may be altered or changed during the process of electronic transmission and consequently none of The Co-operative Bank p.l.c. or either Joint Lead Manager, nor any person who controls either Joint Lead Manager nor any director, officer, employee, agent or affiliate of any such person accepts any liability or responsibility whatsoever in respect of any difference between the Prospectus distributed to you in electronic format herewith and the hard copy version available to you on request from either Joint Lead Manager.

The Co-operative Bank p.l.c.

(*incorporated with limited liability in England with registered number 00990937*)

£250,000,000 Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2025

The issue price of the £250,000,000 Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2025 (the "**Notes**") of The Co-operative Bank p.l.c. (the "**Issuer**" or the "**Bank**") is 100 per cent. of their principal amount.

Unless previously redeemed, purchased or cancelled, the Notes will be redeemed at their principal amount on 1 July 2025 (the "**Maturity Date**"). Subject as provided in Condition 6 (*Redemption and Purchase*), the Notes may be redeemed prior to the Maturity Date at the option of the Issuer in whole but not in part at their principal amount on 1 July 2020. In addition, the Notes may be redeemed at any time in certain limited circumstances upon changes to tax law or regulation or if the entire principal amount of the Notes is fully excluded from qualifying as tier 2 capital under prudential regulatory requirements, all as more particularly described in "*Terms and Conditions of the Notes—Redemption and Purchase*".

From (and including) 1 July 2015 (the "**Issue Date**") to (but excluding) 1 July 2020 (the "**Reset Date**"), the Notes will bear interest at the rate of 8.5 per cent. per annum. From (and including) the Reset Date, the Notes will bear interest at a rate which is the aggregate of 6.53 per cent. per annum and the 5 Year Mid-Swap Rate (as defined herein). Interest will be payable annually in arrear on 1 July each year commencing on 1 July 2016. Payments on the Notes will be made in pounds sterling without deduction for or on account of taxes imposed or levied by the United Kingdom or any political subdivision or any authority thereof or therein having power to tax, except in the circumstances described under "*Terms and Conditions of the Notes—Taxation*".

This Prospectus has been approved by the United Kingdom Financial Conduct Authority (the "**FCA**"), which is the United Kingdom competent authority for the purposes of Directive 2003/71/EC, as amended (the "**Prospectus Directive**") and relevant implementing measures in the United Kingdom as a prospectus issued in compliance with the Prospectus Directive and relevant implementing measures in the United Kingdom for the purpose of giving information with regard to the issue of the Notes. Applications have been made for the Notes to be admitted to listing on the Official List of the FCA and to trading on the regulated market of the London Stock Exchange plc (the "**London Stock Exchange**"). The regulated market of the London Stock Exchange is a regulated market for the purposes of Directive 2004/39/EC on markets in financial instruments.

The Notes have not been, and will not be, registered under the United States Securities Act of 1933 (the "**Securities Act**") and are subject to United States tax law requirements. The Notes are being offered outside the United States by the Joint Lead Managers (as defined in "**Subscription and Sale**") in accordance with Regulation S under the Securities Act ("**Regulation S**"), and may not be offered, sold or delivered within the United States or to, or for the account or benefit of, U.S. persons except pursuant to an exemption from, or in a transaction not subject to, the registration requirements of the Securities Act.

The Notes will be in registered form in denominations of £100,000 and integral multiples of £1,000 in excess thereof. The Notes will, upon issue, be represented by a global registered note certificate (the "**Global Certificate**") registered in the name of The Bank of New York Depository (Nominees) Limited as nominee for, and deposited with, the common depository for Euroclear Bank SA/NV ("**Euroclear**") and Clearstream Banking, *société anonyme* ("**Clearstream, Luxembourg**"). Note certificates in definitive certificated form ("**Note Certificates**") evidencing holdings of Notes will only be available in certain limited circumstances. See "*Summary of Provisions relating to the Notes in Global Form*".

An investment in the Notes involves risk. Prospective investors in the Notes are recommended to read this Prospectus, including the section entitled "*Risk Factors*" carefully.

The Notes will not be rated. The Issuer is rated B (negative outlook) (long-term) and B (short-term) by Fitch Ratings Limited ("**Fitch**") and Caa2 (rating under review for possible downgrade) (long term senior unsecured rating) and NP (short-term) by Moody's Investors Service Ltd ("**Moody's**"). Fitch and Moody's are established in the European Economic Area ("**EEA**") and registered under Regulation (EU) No 1060/2009, as amended (the "**CRA Regulation**"). Fitch and Moody's appear on the latest update of the list of registered credit rating agencies (as of 12 December 2014) on the ESMA website http://www.esma.europa.eu.

A rating is not a recommendation to buy, sell or hold securities and may be subject to suspension, reduction or withdrawal at any time by the assigning rating agency.

Joint Lead Managers

HSBC **UBS INVESTMENT BANK**

29 June 2015

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IMPORTANT NOTICES

The Issuer accepts responsibility for the information contained in this Prospectus and declares that, having taken all reasonable care to ensure that such is the case, the information contained in this Prospectus to the best of its knowledge is in accordance with the facts and contains no omission likely to affect its import.

The Issuer has confirmed to the Joint Lead Managers named under "*Subscription and Sale*" below (the "**Joint Lead Managers**") that this Prospectus contains all information regarding the Issuer and the Notes which is (in the context of the issue of the Notes) material; such information is true and accurate in all material respects and is not misleading in any material respect; any opinions, predictions or intentions expressed in this Prospectus on the part of the Issuer are honestly held or made and are not misleading in any material respect; this Prospectus does not omit to state any material fact necessary to make such information, opinions, predictions or intentions (in such context) not misleading in any material respect; and all proper enquiries have been made to ascertain and to verify the foregoing.

The Issuer has not authorised the making or provision of any representation or information regarding the Issuer or the Notes other than as contained in this Prospectus or as approved for such purpose by the Issuer. Any such representation or information should not be relied upon as having been authorised by the Issuer or the Joint Lead Managers.

Neither the Joint Lead Managers nor any of their respective affiliates have authorised the whole or any part of this Prospectus and none of them makes any representation or warranty or accepts any responsibility as to the accuracy or completeness of the information contained in this Prospectus. Neither the delivery of this Prospectus nor the offering, sale or delivery of any Note shall in any circumstances create any implication that there has been no adverse change, or any event reasonably likely to involve any adverse change, in the condition (financial or otherwise) of the Issuer since the date of this Prospectus.

This Prospectus does not constitute an offer of, or an invitation to subscribe for or purchase, any Notes.

The distribution of this Prospectus and the offering, sale and delivery of Notes in certain jurisdictions may be restricted by law. Persons into whose possession this Prospectus comes are required by the Issuer and the Joint Lead Managers to inform themselves about and to observe any such restrictions. For a description of certain restrictions on offers, sales and deliveries of Notes and on distribution of this Prospectus and other offering material relating to the Notes, see "*Subscription and Sale*".

In particular, the Notes have not been and will not be registered under the Securities Act and are subject to United States tax law requirements. Subject to certain exceptions, Notes may not be offered, sold or delivered within the United States or to U.S. persons.

The Notes are subordinated capital securities of the Bank and are not protected by the Financial Services Compensation Scheme (the "**FSCS**"). The Notes will, upon issue, form part of the regulatory capital of the Bank. Banks are required to hold regulatory capital to absorb losses (before depositors and other senior creditors suffer losses), including during periods of financial stress. As a provider of capital to the Bank, an investor in the Notes should be prepared to suffer losses on its investment if, in particular, the Bank and/or the financial sector generally approaches or enters into a period of financial stress. Such losses could be manifested in a number of ways, including (without limitation) that the market price of the Notes may fall significantly, the United Kingdom authorities could take action under the Banking Act 2009 as amended from time to time (the "**Banking Act**") (or similar future legislation), or the Bank could enter into an insolvent winding-up, with the result that investors in the Notes could lose all or substantially all of their initial investment in the Notes. Since the Notes are not protected by the FSCS, the FSCS will not pay any compensation to an investor under these, or any other, circumstances. Accordingly, an investor in the Notes may lose some, or the entire amount of, its investment in the Notes.

In this Prospectus, unless otherwise specified, references to a "**Member State**" are references to a Member State of the European Economic Area and references to "**£**", "**GBP**", "**sterling**", "**Sterling**" or "**pounds sterling**" are to the lawful currency of the United Kingdom.

Certain figures included in this Prospectus have been subject to rounding adjustments; accordingly, figures shown for the same category presented in different tables may vary slightly and figures shown as totals in certain tables may not be an arithmetic aggregation of the figures which precede them.

In connection with the issue of the Notes, the Joint Lead Manager or Joint Lead Managers acting as the Stabilising Manager(s) (the "Stabilising Manager(s)") (or persons acting on behalf of the Stabilising Manager(s)) may over allot Notes or effect transactions with a view to supporting the price of the Notes at a level higher than that which might otherwise prevail. However, there is no assurance that the Stabilising Manager(s) (or persons acting on behalf of a Stabilising Manager) will undertake stabilisation action. Any stabilisation action may begin on or after the date on which adequate public disclosure of the terms of the offer of the Notes is made and, if begun, may be ended at any time, but it must end no later than the earlier of 30 days after the issue date of the Notes and 60 days after the date of the allotment of the Notes. Any stabilisation action or over-allotment must be conducted by the Stabilising Manager(s) (or persons acting on behalf of the Stabilising Manager(s)) in accordance with all applicable laws and rules.

INFORMATION INCORPORATED BY REFERENCE

The information set out in the table below shall be deemed to be incorporated in, and to form part of, this Prospectus **provided however that** any statement contained in any document incorporated by reference in, and forming part of, this Prospectus shall be deemed to be modified or superseded for the purpose of this Prospectus to the extent that a statement contained herein modifies or supersedes such statement.

The documents containing the information incorporated by reference will be made available, free of charge, during usual business hours at the registered office of the Issuer at 1 Balloon Street, Manchester M60 4EP and on the Issuer's website at https://www.co-operativebank.co.uk/investorrelations.

For ease of reference, the tables below set out the relevant page references, within the relevant documents, of the information which is incorporated by reference into this Prospectus, and which include the financial statements, the notes to the financial statements and the Auditors' reports for the years ended 2014 and 2013 for the Issuer, as set out in the respective annual reports.

(a) From the Issuer's 2013 annual report (the "**2013 Annual Report**") at the following pages:

Auditor's report and audited consolidated annual financial statements of the Issuer for the financial year ended 31 December 2013

Auditor's Report	Pages 124 – 126
Consolidated Income Statement	Page 128
Consolidated Statement of Comprehensive Income	Page 129
Consolidated Balance Sheet	Page 130
Consolidated Statement of Cashflows	Pages 131 – 132
Consolidated Statement of Changes in Equity	Page 133
Notes to Financial Statements	Pages 134 – 219

Capital management

Capital Management	Pages 117 – 121

(b) From the Issuer's 2014 annual report (the "**2014 Annual Report**") at the following pages:

Auditor's report and audited consolidated annual financial statements of the Issuer for the financial year ended 31 December 2014

Auditor's Report	Pages 140 – 146
Consolidated Income Statement	Page 148
Consolidated Statement of Comprehensive Income	Page 149
Consolidated Balance Sheet	Page 150
Consolidated Statement of Cashflows	Pages 151 – 152
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Financial review, risk management and capital management

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Except as set forth above, no other portion of the aforementioned documents is incorporated by reference into this Prospectus and any information contained in such documents which is not incorporated by reference in this Prospectus is either not relevant for the investor or is covered elsewhere in this Prospectus. Any documents and/or information themselves incorporated by reference in the documents incorporated by reference in this Prospectus shall not form part of this Prospectus.

OVERVIEW

This overview must be read as an introduction to this Prospectus and any decision to invest in the Notes should be based on a consideration of the Prospectus as a whole, including the information incorporated by reference.

Words and expressions defined in the "Terms and Conditions of the Notes" below or elsewhere in this Prospectus have the same meanings in this overview.

The Issuer:	The Co-operative Bank p.l.c. The Bank is a public limited company, incorporated and domiciled in the UK with its registered office situated in England and Wales. The Bank operates under the Companies Act 2006 (the "**Companies Act**") is authorised by the UK Prudential Regulation Authority (the "**PRA**") and is regulated by the PRA and the FCA. The Bank's Firm Reference Number is 121885. The registered address and head office of the Bank is at P.O. Box 101, 1 Balloon Street, Manchester, M60 4EP (telephone number: +44 161 832 3456).
Joint Lead Managers:	HSBC Bank plc and UBS Limited.
Trustee:	Law Debenture Trustees Limited.
Registrar:	The Bank of New York Mellon (Luxembourg) S.A.
Principal Paying Agent and Calculation Agent:	The Bank of New York Mellon, London Branch.
The Notes:	£250,000,000 Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2025.
Issue Price:	100 per cent. of the principal amount of the Notes.
Issue Date:	1 July 2015.
Interest:	The Notes will bear interest from (and including) the Issue Date to (but excluding) the Reset Date at a rate of 8.5 per cent per annum. From (and including) the Reset Date, the Notes will bear interest at a rate which is the aggregate of the initial margin of 6.53 per cent. and the 5 Year Mid-Swap Rate on the date that is two Business Days prior to the Reset Date, converted by the Calculation Agent from a semi-annual to an annual basis in a commercially reasonable manner. Interest will be payable annually in arrear on 1 July in each year commencing 1 July 2016.
Status:	The Notes will constitute direct, unsecured and subordinated, obligations of the Issuer, ranking *pari passu* without any preference among themselves and on a winding-up of the Issuer claims in respect of the Notes shall rank: (i) at least *pari passu* with all claims of holders of all other subordinated obligations of the Issuer which constitute, and all claims relating to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which constitute, or (in either case) would but for any applicable limitation on the amount of such capital constitute, Tier 2 Capital and all obligations which rank, or are expressed to rank, *pari passu* therewith; and (ii) in priority to the claims of holders of (a) all obligations of the Issuer which rank or are expressed to rank, and all claims relating

to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which rank or are expressed to rank, junior to the claims in respect of the Notes, including (without limitation) obligations which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 1 Capital and all obligations which rank, or are expressed to rank, *pari passu* therewith; and (b) all classes of share capital of the Issuer,

as more fully described in Condition 3 (*Status and Subordination of the Notes*).

Form and Denomination: The Notes will be issued in registered form in denominations of £100,000 and integral multiples of £1,000 in excess thereof. The Notes will, upon issue, be represented by a Global Certificate registered in the name of The Bank of New York Depository (Nominees) Limited as nominee for, and deposited with, the common depository for Euroclear and Clearstream, Luxembourg. Note Certificates in definitive form evidencing holdings of Notes will only be available in certain limited circumstances – see "*Summary of Provisions relating to the Notes in Global Form*".

Maturity Date: 1 July 2025.

Optional Redemption: Subject as provided in Condition 6.2 (*Redemption on the Reset Date at the option of the Issuer*) and Condition 6.7 (*Redemption and Purchase Conditions*), the Notes may be redeemed at the option of the Issuer on 1 July 2020 in whole but not in part, at their principal amount together with any accrued but unpaid interest to (but excluding) the Reset Date.

Tax Redemption: Subject as provided in Condition 6.3 (*Redemption for Tax Reasons*) and Condition 6.7 (*Redemption and Purchase Conditions*), if at any time a Tax Event occurs, the Issuer may redeem all, but not some only, of the Notes at any time at their principal amount together with any accrued but unpaid interest to (but excluding) the date of redemption, all as more particularly described in "*Terms and Conditions of the Notes—Redemption and Purchase*".

Regulatory Event Redemption: Subject as provided in Condition 6.4 (*Regulatory Event Redemption*) and Condition 6.7 (*Redemption and Purchase Conditions*), if at any time a Regulatory Event occurs, the Issuer may redeem all, but not some only, of the Notes at their principal amount together with any accrued but unpaid interest to (but excluding) the date of redemption, all as more particularly described in "*Terms and Conditions of the Notes—Redemption and Purchase*".

Events of Default and Enforcement: The rights of enforcement of the holders of Notes are limited. In particular, payment obligations of the Issuer can be enforced, and the Notes are capable of being accelerated, only in a winding-up of the Issuer. See Condition 9 (*Events of Default and Enforcement*).

Rating: The Notes will not be rated. The Issuer is rated B (negative outlook) (long-term) and B (short term) by Fitch and Caa2 (rating under review for possible downgrade) (long term senior unsecured rating) and NP (short-term) by Moody's. Fitch and Moody's are established in the EEA and registered under the CRA Regulation. Fitch and Moody's appear on the list of registered credit rating agencies on the ESMA website at http://www.esma.europa.eu.

In general, European regulated investors are restricted from using a rating for regulatory purposes if such rating is not issued by a credit

	rating agency established in the EEA and registered under the CRA Regulation unless (1) the rating is provided by a credit rating agency not established in the EEA but is endorsed by a credit rating agency established in the EEA and registered under the CRA Regulation or (2) the rating is provided by a credit rating agency not established in the EEA which is certified under the CRA Regulation.
Withholding Tax:	All payments of principal and interest in respect of Notes by the Issuer will be made without withholding or deduction for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the United Kingdom or any political subdivision or any authority thereof or therein having power to tax, unless such withholding or deduction is required by law. In the event that any such deduction is made, the Issuer will, save in certain limited circumstances, be required to pay additional amounts to cover the amounts so deducted, all as described in Condition 7 (*Taxation*).
Governing Law:	The Notes, the Trust Deed, the Agency Agreement, the Subscription Agreement and any non-contractual obligations arising out of or in connection with them will be governed by, and construed in accordance with, English law.
Listing and Trading:	Applications have been made for the Notes to be admitted to listing on the Official List of the FCA and to trading on the regulated market of the London Stock Exchange.
Clearing Systems:	Euroclear and Clearstream, Luxembourg.
Selling Restrictions:	United States (Regulation S, Category 2) and the United Kingdom. See "*Subscription and Sale*".
Risk Factors:	Investing in the Notes involves risks. See "*Risk Factors*".

RISK FACTORS

Any investment in the Notes is subject to a number of risks. Prior to investing in the Notes, prospective investors should carefully consider risk factors associated with any investment in the Notes, the business of the Issuer and the industry in which it operates together with all other information contained in this Prospectus, including, in particular the risk factors described below. Words and expressions defined in the "Terms and Conditions of the Notes" below or elsewhere in this Prospectus have the same meanings in this section.

The Issuer believes that the factors described below represent the principal risks involved in investing in the Notes, but the Issuer may be unable to pay interest, principal or other amounts on or in connection with the Notes for other reasons, and Issuer does not represent that the statements below regarding the risks of holding the Notes are exhaustive. Additional risks and uncertainties relating to the Issuer that are not currently known to the Issuer or that it currently deems immaterial, may individually or cumulatively also have a material adverse effect on the business, prospects, results of operations and/or financial position of the Issuer and, if any such risk should occur, the price of the Notes may decline and investors could lose all or part of their investment. Investors should consider carefully whether an investment in the Notes is suitable for them in light of the information in this Prospectus and their personal circumstances.

Risks relating to the Bank

A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements

Background

In November 2013, the Bank adopted a four to five year business plan and began to implement a range of measures aimed at improving its financial and operational performance and capital position. These included measures intended to improve its capital position (for example the Recapitalisation Plan which included the Liability Management Exercise); and measures intended to improve its operational performance (for example separating its Non-core Business from its Core Business and refocusing the Core Business on its core relationship with retail and small to medium-sized enterprises ("**SME**") banking customers, overseeing a run-off and exit of its Non-core Assets over the medium term, and embarking on a significant cost reduction programme across the Bank).

The Recapitalisation Plan and Liability Management Exercise are each defined and further described in paragraph 1 (*Overview*) of the section entitled "*Description of the Bank*", and Non-core Business, Core Business and Non-core Assets are each defined and further described in paragraph 3 (*Business Overview*) of the section entitled "*Description of the Bank*".

Since December 2013, the Bank has identified additional conduct and legal issues, resulting in the starting capital position of the Bank for the recovery period being weaker than in the plan adopted in November 2013. To remedy the consequent deficit in, and to further strengthen, the Bank's regulatory capital position, the Bank raised £400 million through the issue of additional common stock, qualifying as common equity tier 1 ("**CET1**") capital, in May 2014. This has enabled the Bank to continue with the execution of its business plan.

In December 2014, the PRA announced the results of the Bank of England stress tests and confirmed that the Bank's capital resources were projected to be exhausted in the Bank of England's hypothetical stress scenario and therefore the Bank did not meet the requirements of the stress test scenario. As a result the Bank was required to submit a revised business plan to demonstrate that it could deliver a level of resilience required for a bank of its planned future size and business model to withstand the stress test scenario by the end of the planning period. This revised business plan was accepted by the PRA. The Bank's revised business plan, which runs from 2015 to 2019 (the "**planning period**", "**plan period**" or "**period of the plan**") does not change the Bank's overarching strategy, but it does look to accelerate the deleveraging of the Non-core Business, and in particular, the Optimum residential mortgage portfolio of loans, with a view to significantly improving the Bank's resilience to a stress test as severe as the one run by the Bank of England in 2014, towards the end of the revised plan and maintaining the required capital ratios under the aforementioned stress by that time. As part of this deleveraging, on 6 May 2015, the Bank

successfully closed its inaugural whole capital structure securitisation of approximately £1.5 billion comprising part of the Optimum residential mortgage portfolio of loans through Warwick Finance Residential Mortgages Number One PLC ("**Warwick Finance One**").

Strategic Plan Implementation Risk

The Bank's revised business plan was developed in a relatively short timeframe and is in the early stages of implementation. Its performance and effectiveness are not yet proven. There is a risk that the Bank's strategy to deliver the revised business plan may be insufficient to address the Bank's problems or deliver the projected benefits. The successful execution of the Bank's strategy requires the simultaneous execution of a number of complex and overlapping projects involving significant changes to the Bank's systems and operations, in a manner that does not impact negatively upon the Bank's brand, reputation, customer satisfaction or its relationships with, and ability to retain, its employees. The Bank does not have a track record of successfully executing large-scale changes as contemplated by its revised business plan and similar projects have failed in the past, resulting in large write-offs and lost opportunities. Changes required to execute the Bank's strategy include:

- the finalisation of the separation arrangements between the Bank and the Co-operative Group following the Liability Management Exercise;
- the implementation of significant cost reductions;
- remediation of the IT estate on an accelerated time-scale and implementation of a new IT strategy in the long term;
- the reorientation of its distribution network;
- improving revenue in its business over the medium term;
- the outsourcing of significant business processes and systems;
- a streamlining of its product offering to improve efficiency of the Bank's operations; and
- an accelerated deleverage of its Non-core Assets, and in particular the Optimum residential mortgage portfolio of loans, in a manner intended to provide economic stress resilience to the Bank and achieve optimal economic outcomes (after taking into consideration capital requirements, liquidity provisions, the nature of the assets and the underlying trends of value of such assets).

Strategic Plan Implementation Risks Examples

Many of the risk factors relating to the Bank and its business set out in this Prospectus could have a significant adverse impact on the Bank's ability to deliver the above changes and its strategy. For example:

- the separation project is complex and may be more costly than originally contemplated. Any new arrangements may be less favourable to the Bank than the existing arrangements. Further costs or cost increases, delays and other execution problems regarding the separation could impact the Bank's ability to implement its strategy;
- the implementation of significant cost reductions, for example through branch closures, redundancies and the reorientation of the Bank's distribution channels and simplification of the Bank's product offering, may not achieve the targeted cost savings. However, reduced revenue expectations may adversely impact any forecast cost-income ratio targets;
- the Bank's strategy includes leveraging the Bank's differentiated brand and commitment to customer satisfaction and is dependent on retaining customers. Implementation of cost savings may have a negative impact on the Bank's brand, customer service and levels of satisfaction and therefore its income. There are a number of on-going investigations into, or connected with, the Bank and the outcome of these and other issues may impact upon the Bank's reputation and may have a negative impact on the Bank's brand and its ability to deliver its revised business plan;

- the required remediation and improvement of the Bank's IT estate and the migration away from reliance on the Co-operative Group's IT services is significant in its urgency, scale, complexity and cost. Any delays in, or failure by, the Bank to deliver these technology changes may extend an on-going risk of technology failure, significant additional investment cost, subject the Bank to further regulatory scrutiny which may result in the PRA and/or the FCA taking immediate supervisory intervention or exercising any of their regulatory powers in relation to any existing and future breaches of threshold conditions and impact the Bank's ability to deliver its business strategy. The act of remediating and migrating the systems itself involves a number of risks. The Non-core Business and the Core Business share critical technology components within the IT estate. As the IT estate is remediated, migrated and improved in line with the Core Business strategy, IT systems may, over time, cease to be suitable for the activities of the Non-core Business. See also risk factor entitled "*The Bank's operations are highly dependent on the proper functioning of IT and communication systems which are currently in need of urgent and extensive remediation. Any significant delay in or failure of the Bank to remedy the existing IT estate and make improvements in it to meet the requirements of its business strategy may adversely affect the future operational and financial performance of the business. The Bank's disaster recovery plan for this IT infrastructure has not been proven, creating a material resilience risk*";

- any outsourcing of the Bank's systems and processes to a third party may have a negative impact on the Bank's brand, customer service and levels of satisfaction and therefore its income. In addition the failure to successfully implement significant outsourcing programmes carries the risk of increased project costs and reduced cost savings;

- the Bank's ability to improve revenue in its Core Business through improved pricing of its products, appropriate re-pricing of existing products towards market rates, growing customers in the Bank's key market segments, cross-selling products and growing the volume of higher margin unsecured lending is dependent upon a number of factors. For example, ensuring that the Bank has products that comply with legal and regulatory requirements and are fit for purpose, prevailing macroeconomic conditions (including the level of interest rates and/or non-interest income), the Bank's relative position versus its competitors, the Bank's brand and reputation, the acquisition and retention of customers and the ability of persons working for the Bank to cross-sell products appropriately;

- in December 2014, the Bank submitted a revised business plan to the PRA which has been accepted by the PRA and runs from 2015 to 2019. Once delivered, it will help the Bank to comply with FCA and PRA regulatory requirements or expectations. The Bank has had various deficiencies against regulatory requirements or expectations which have existed for some time and will continue for some years to come while the Bank executes its revised business plan. The revised business plan anticipates that the Bank will meet the minimum 7 per cent. CET1 ratio throughout the planning period (2015 to 2019) and, although the Bank may not always, throughout the period of the revised business plan, meet its Individual Capital Guidance ("**ICG**"), the Bank expects to be fully in compliance with its ICG requirements by the end of such planning period. The revised business plan aims to build a sustainable core bank and is designed to create a capital planning buffer ("**CPB**") by 2019 which would withstand a severe stress scenario equivalent to the 2014 Bank of England stress test. The ability of the Bank to raise funds through the issuance of the Notes and other capital raisings in the future, and while such deficiencies exist, which the Bank has assumed in the revised business plan, will be taken into account by the PRA. To move forward with the Bank's revised business plan, the Bank requires the PRA and/or the FCA's ongoing acceptance of its inability to meet regulatory requirements and expectations, including ICG. To the extent that this is not forthcoming or to the extent that the Bank does not perform in line with its revised business plan or regulatory requirements are increased for any reason, additional CET1 capital may be required over and above that included in that plan. Any failure to raise such further capital could have a material adverse effect on the Bank's regulatory capital position including its ability to maintain adequate loss-absorbing capacity (see also risk factor entitled " – *The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by it not maintaining adequate regulatory capital, by future changes to its regulatory capital requirements and by changes to PRA expectations in respect of capital adequacy*" below). Continued failure by the Bank to meet some of its capital requirements (including its ICG), would impact the actions that the management are able to take to implement the revised business plan and may lead to the PRA

exercising some or all of its powers over the Bank, including powers of intervention, and, in severe circumstances, the UK resolution authorities could elect to exercise powers to write down or bail-in capital securities (including the Notes) and to implement resolution procedures if they consider the Bank would otherwise be likely to fail (see also risk factor entitled "*The continued existence of one or more areas of non-compliance by the Bank with respect to certain regulatory and prudential capital requirements may expose the Bank to an increased risk of actions that may be taken by the regulatory authorities under the UK Banking Act as part of a special resolution regime")*;

- a failure to deliver the accelerated deleverage of the Bank's Non-core Assets in a capital efficient manner may have a negative impact on the Bank's business, operating results, financial condition (including its net interest margin), continued viability in the medium term and its ability to comply with its regulatory capital requirements;

- the Bank's business and financial performance have been and may continue to be affected by general economic conditions in the UK and adverse developments in the UK or global financial markets could cause the Bank's earnings and profitability to decline;

- the total amount owed by the Co-operative Group to the Bank is the largest single counterparty exposure of the Bank. The exposure is not insubstantial and, in the normal course of events, this would significantly exceed the Bank's risk appetite. However, the facilities have been structured to minimise the impact of any credit deterioration in the counterparty. The banking relationship is a historical one and the exposure has been managed within the limits set. In addition, any failure of the Co-operative Group to provide any other services or functions upon which the Bank is dependent would have an adverse effect on the business and operations of the Bank.

The successful development and implementation of the Bank's strategy requires difficult, subjective and complex judgements including about a range of factors which are not within the Bank's control, e.g. forecasts of economic conditions. Furthermore, the successful implementation of the Bank's strategy is contingent upon a range of factors which are beyond the Bank's control, including market conditions, the general business environment, regulation (including currently unexpected regulatory change), the activities of its competitors and consumers and the legal and political environment. The auditor's reports in the financial statements for years ended 31 December 2013 (on page 124 of the 2013 Annual Report) and 31 December 2014 (on pages 140 and 141 of the 2014 Annual Report) each contain an "emphasis of matter" in relation to the Bank's and its group's (as defined therein) ability to continue as a "Going Concern". While the Directors are satisfied that the Bank and its group have sufficient resources to continue in business for the foreseeable future (being the period of at least 12 months from the date of signing of the auditor's report (being 26 March 2015) in respect of the financial statements of the Bank for the year ended 31 December 2014), the Going Concern status of the Bank (which has been adopted in preparing its financial statements for the year ended 31 December 2014) is dependent on successful execution of the Bank's strategy, which remains subject to the risks as described above in this risk factor.

High operating costs, credit impairment, higher than expected conduct provisions and one-off costs have significantly impacted the Bank's profitability. The Bank expects to be loss making at least through 2015 and 2016

The Bank's statutory loss before taxation at 31 December 2014 was £225.2 million. Although this loss is considerably less than the Bank's statutory loss of £777.3 million for the year ending 31 December 2013, the loss remains significant. There remain a number of challenges to profitability ahead, including a continuing need to control and reduce the cost base, generate additional Core Business income and complete the separation from the Co-operative Group. The Bank expects to be loss making at least through 2015 and 2016. See the risk factors entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*" and paragraph 10 (*Loss Forecast*) of the section entitled "*Description of the Bank*" for further information.

The continued existence of one or more areas of non-compliance by the Bank with respect to certain regulatory and prudential capital requirements may expose the Bank to an increased risk of actions that may be taken by the regulatory authorities under the UK Banking Act as part of a special resolution regime

The Bank is currently non-compliant with respect to certain regulatory and prudential capital requirements as described above in these Risk Factors. In summary, these areas of non-compliance comprise ICG non-compliance, capital planning buffer non-compliance, regulatory reporting non-compliance under solo consolidation permission, CRR attestation compliance in relation to current IRB permissions and FCA Threshold Conditions breach with respect to IT (non-financial resources). Please refer to the risk factors entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*", "*The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by it not maintaining adequate regulatory capital, by future changes to its regulatory capital requirements and by changes to PRA expectations in respect of capital adequacy*", "*Solo Consolidation*", "*The Bank's policies and processes for risk management may prove inadequate for the risks faced by its business. Any failure to properly manage the risks which it faces could cause harm to the Bank and its business prospects*", "*The Bank's operations are highly dependent on the proper functioning of IT and communication systems which are currently in need of urgent and extensive remediation. Any significant delay in or failure of the Bank to remedy the existing IT estate and make improvements it to meet the requirements of its business strategy may adversely affect the future operational and financial performance of the business. The Bank's disaster recovery plan for this IT infrastructure has not been proven, creating a material resilience risk*".

While the Bank has agreed to a revised business plan with the PRA in order to address some of these deficiencies, failure to implement the revised business plan may lead to the PRA, at its discretion, electing to exercise one or more of its various powers over the Bank. This could include a variation of the Bank's permissions, restricting the Bank's business or, in conjunction with the other UK resolution authorities, imposing a write-down of the Bank's regulatory capital instruments and, potentially, the commencement of a wider resolution procedure in respect of the Bank, particularly if it were satisfied that the Bank is failing, or is likely to fail. Pursuant to section 7 of the Banking Act, a UK bank will be considered as failing or likely to fail when, but for financial assistance (if any) provided by HM Treasury or the Bank of England (disregarding ordinary market assistance offered by the Bank of England on its usual terms): it is, or is likely in the near future to be, failing, or likely to fail, to satisfy the PRA Threshold Conditions where such failure would justify the variation or cancellation of the relevant UK bank's permission under FSMA to carry on one or more regulated activities; the value of its assets is, or is likely in the near future to be, less than its liabilities; it is, or is likely in the near future to be, unable to pay its debts or other liabilities as they fall due; or it requires extraordinary public financial support (and such support does not fall within certain limited circumstances). In addition, the Bank has received written confirmation from the FCA that the Bank not having a proven end-to-end disaster recovery capability constitutes a breach of the FCA Threshold Conditions. The FCA is closely supervising the Bank as it works towards restoring compliance with COND 2.4 of the FCA Threshold Conditions as they relate to non-financial resources. The FCA is not currently proposing further immediate supervisory intervention or the immediate exercise of any additional regulatory powers as a result of this assessment, and reserves the right to take action in the future in relation to this breach. Both the PRA and FCA are closely monitoring the position of the Bank and the Bank remains in continual dialogue with both regulators. However, there is a risk that the FCA and/or the PRA may take immediate supervisory intervention or exercise any of their regulatory powers in relation to this breach.

The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by it not maintaining adequate regulatory capital, by future changes to its regulatory capital requirements and by changes to PRA expectations in respect of capital adequacy

For most of 2014, the Bank was not compliant with its ICG. On 31 December 2014, the final capital injection of the aggregate one-off £333 million contribution from CBG (as defined in "*Description of the Bank — 1. Overview*"), as part of the Recapitalisation Plan, helped push the Bank into ICG compliance. However, due to the Bank's ongoing losses, this position should be regarded as temporary. Although the Bank may not always, throughout the planning period, meet its ICG requirements (being the PRA's statement as to the regulatory capital (Pillar 2a) that it expects the Bank to hold above Pillar 1), the Bank

expects to be fully in compliance with its ICG requirements by the end of the planning period. The Bank met the Pillar 1 requirement throughout 2014 and expects to continue to do so.

The PRA has accepted the Bank's revised business plan which anticipates that the Bank will be resilient to a stress test as severe as the one run by the Bank of England in 2014 towards the end of the revised plan. The revised business plan still envisages that the Bank will raise approximately £400 million of additional capital not regarded as CET1 capital. This is expected to be completed in the early stages of the planning period and the issue of the Notes forms a part of this £400 million of additional capital. The Bank believes that both this issue of the Notes and further expected issuance (in aggregate up to £400 million) will be required to maintain the Bank's eligible liabilities position (under future MREL (as defined below) requirements yet to be set by or implemented in the UK) following the maturity in October 2015 of the euro 500 million of senior unsecured debt issued under the Bank's euro medium term note programme. It is expected that, once such additional capital is delivered, it will help the Bank to comply with FCA and PRA regulatory requirements and expectations in further strengthening the Bank's total regulatory capital base and (MREL) eligible liabilities. In the event the Bank is unable to raise all or part of such additional capital, there is a risk that the regulatory authorities could require further or other actions to be taken by the Bank. It is expected that any actions required would be measured against other Bank metrics relevant at the time including the current performance of the Bank and the impact of the Bank's continued deleverage programme of the Optimum residential mortgage portfolio as to relevant regulatory capital requirements. In the event that other actions were unable to be taken by the Bank, the regulatory authorities would be able to take further actions under the range of options available to them, including special resolution under the SRR of the BRRD. See also the risk factors entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements – Strategic Plan Implementation Risks Examples*" above; and "*Risks relating to the Notes – The Bank is subject to the UK Banking Act. The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK banks and certain of their affiliates in the event a bank in the same group is considered to be failing or likely to fail. Furthermore, such actions can be taken directly against any relevant entity or against certain of its UK group companies. The exercise of any of these actions in relation to the Bank could materially adversely affect the value of the Notes, or could result in the principal amount of the Notes being written down or written off entirely*" below.

The Bank expects the CET1 ratio to temporarily increase during 2015 from its current level at year end 2014, primarily as a result of the securitisation of part of the Optimum residential mortgage portfolio. It is expected to decline thereafter before subsequently recovering. As a result, the leverage ratio is not expected to be consistently above 3 per cent. until the latter stages of the planning period.

The threshold conditions for which the PRA is responsible (the "**PRA Threshold Conditions**") in relation to the Bank are set out in paragraphs 5A to 5F of Schedule 6 of the Financial Services and Markets Act 2000, as amended ("**FSMA**"). The PRA's general policy is not to communicate its assessment of its position in relation to the PRA Threshold Conditions. The PRA has not communicated to the Bank its assessment of the Bank's position in relation to the PRA Threshold Conditions.

Whether the Bank is able to meet its ICG during the period of the plan will depend on a number of factors, both within and outside the control of the Bank, including the Bank's ability to implement its revised business plan and changes in regulatory risk appetite and economic and market conditions generally in the UK. See the risk factor entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*" for further information. While the PRA has acknowledged the Bank's revised business plan to meet the stress scenario run by the Bank of England in 2014, the PRA has the discretion to revisit the Bank's capital requirements and the Bank's non-compliance with its ICG. It is not possible to predict with any degree of certainty if, and, therefore, when, the PRA would revisit them and, if so, the nature or extent of any possible changes to the ICG or capital requirements. Should the Bank fail to meet its ICG or its plan to comply with its ICG, it is not possible to predict how the PRA would react. The PRA may, in any such circumstances, at its discretion elect to exercise one or more of its various powers over the Bank. This could include a variation of the Bank's permissions, restricting the Bank's business or, in conjunction with the other UK resolution authorities, imposing a write-down of the Bank's regulatory capital instruments and, potentially, the commencement of a wider resolution procedure in respect of the Bank. There is a risk that the Bank's regulatory capital requirements or PRA expectations

and approach with respect to such capital requirements may increase beyond those currently planned for by the Bank.

Solo Consolidation

Until its expiry in September 2014, the Bank had regulatory approval to operate under a 'solo-consolidation' permission, which allowed it to be regulated for prudential purposes as though the Bank and specified solo-consolidated subsidiaries formed a single legal entity. In March 2015, the Bank was granted a new permission to apply solo-consolidation, though with respect to a smaller number of subsidiaries. Currently, the Bank and its subsidiaries do not have the processes in place to comply with regulatory reporting obligations resulting from this change, or with large exposure requirements in respect of exposures to certain FCA-authorised subsidiaries. However, the Bank intends to address these issues to a timetable set by the regulators. The Bank has already acted to ensure its FCA-authorised subsidiaries comply with capital requirements on an individual basis.

The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by future changes to its regulatory capital requirements driven by regulatory stress testing results

In December 2014, the PRA announced the results of the Bank of England stress tests and confirmed that the Bank’s capital resources were projected to be exhausted in the Bank of England's hypothetical stress scenario and therefore the Bank did not meet the requirements of the stress test scenario. As a result, the Bank was required to submit a revised business plan to deliver capital resilience against the stress scenario. The revised business plan aims to build a sustainable core bank and is designed to create a capital planning buffer by 2019 which would withstand a severe stress scenario equivalent to the 2014 Bank of England stress test.

A key source of vulnerability in the stress scenario, relating to a severe housing-related stress scenario, stems from the Bank’s Non-core Business and in particular, the Optimum residential portfolio of loans. For further information, please refer to the risk factor entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*" above.

In March 2015, the Bank of England announced some details of the Bank of England 2015 stress test. The Bank was not asked to participate in the 2015 stress test as the Bank (i) has a smaller balance sheet than in 2014; (ii) will have a more limited role in payment systems in the future; (iii) has no plans to grow the size of its balance sheet; and (iv) is significantly smaller than the other banks included in the 2015 stress test. It is not possible for the Bank to predict whether or not it will be required to participate in future stress tests or what form and magnitude of future stress tests may be applied to it and, if required to do so, what balance sheet actions may be required to mitigate any assumed stress impacts.

There may be future capital calls as a result of regulatory requirements or guidance or as a result of further costs or losses exceeding the Bank's estimates and assumptions underlying its business plan contained in its business plan

The issue of the Notes is being undertaken in anticipation of current regulatory requirements and the amount being raised is based on certain assumptions being made in the Bank's business plan. There is no guarantee that the PRA will not enforce stricter regulatory capital requirements on the Bank (whether specifically applicable to the Bank or to banks more generally), resulting in a need for the Bank to raise further capital. Future capital calls may also be required as a result of further costs or losses or shortfall in revenues exceeding the Bank's estimate. The Bank may be unable to raise any additional capital it may need on favourable terms, when needed or at all. In such cases, the Bank may breach its regulatory requirements or expectations and there may be a risk of the PRA exercising any of its wide-ranging powers over the Bank, including resolution under the Banking Act.

The Bank is operationally dependent on the Co-operative Group and has significant counterparty exposure to the Co-operative Group. Further deterioration or perceived deterioration in the soundness of the Co-operative Group may have a material adverse effect on the Bank's business, financial condition, operating results, reputation and prospects

Given the high level of interdependence between the Bank and the Co-operative Group, the Bank is and will continue to be subject to the risk of deterioration of the commercial and financial soundness or perceived soundness of the Co-operative Group which was, until conclusion of the Liability Management Exercise in December 2013, the Bank's parent undertaking. To the extent that the Co-operative Group is prevented from or is or becomes unable to meet its obligations towards the Bank, this could lead to significant operational risks, capital and liquidity requirements.

The Bank is dependent upon the Co-operative Group taking a number of actions or decisions in a variety of different capacities, including as a shareholder, debtor, customer and supplier. A number of these actions or decisions could require the approval of the Co-operative Group's board and/or the consent of its banking syndicate. Consequences may include: failure of customers to distinguish between the Co operative Group's brand and the Bank's brand and reliance upon the "Co-operative" brand; failure to protect employee/customer information while, for example, the Bank and the Co-operative Group continue to share IT infrastructure; exposure to The Co-operative Pension Scheme ("**Pace**") and changes in accounting for Pace; and the process of separation from the Co operative Group and the complexities surrounding this.

A weakened position of the Co-operative Group, or deterioration in the soundness of the Co-operative Group or the Bank's former sister company, CFS Management Services Limited ("**CFSMS**") may have a material adverse effect on the Bank's business, financial condition, operating results, reputation and prospects.

The financial services industry continues to be the focus of significant legislative and regulatory change which has and could continue to impose operational restrictions on the Bank, increase the Bank's costs and/or capital requirements and/or otherwise materially adversely affect its business, operating results, financial condition and prospects

Regulators and other bodies in the UK and worldwide have implemented and continue to consider a range of legislative and regulatory changes. These include, amongst others:

- *Measures at UK level*
    - prudential capital and liquidity requirements. Several elements of the Basel III framework (implemented in the European Union as Directive 2013/36/EU ("**CRD IV**") and as Regulation (EU) No 575/2013 ("**CRR**")) of reforms remain subject to on-going review, potential adjustment and uncertainty as to their application within the European Union, the UK generally and to the Bank specifically. CRD IV and CRR have already introduced significant changes in the prudential regulatory regime applicable to banks, including changes to limits on large exposures, the allocation of capital surcharges to globally and locally systemically important banks, the application of systemic risk buffers to banks by Member States, additional liquidity requirements to supplement the Liquidity Coverage Ratio ("**LCR**") and potential amendments to the leverage ratio. In 2014, the UK Financial Policy Committee ("**FPC**") consulted on revisions to the UK implementation of the leverage ratio, and published its final review on 31 October, 2014 setting out its proposals for the design of the leverage ratio framework, including its views on the calibration of that framework; it is currently unclear whether the implementation of any such proposals could adversely impact the Bank's compliance with leverage ratio requirements, and adversely impact the Bank's profitability if, as a result, it is necessary to issue Additional Tier 1 capital securities or to raise further CET1 capital.
    - measures contained in the Financial Services (Banking Reform) Act 2013 (the "**Banking Reform Act**"). These include provisions that allow HM Treasury to implement the main reforms recommended by the UK Independent Commission on Banking including but not limited to:

- the separation of the UK and EEA retail banking activities of the largest UK banks into a legally, operationally and economically separate and independent entity (so called 'ring fencing');
- a reserve power for the PRA to enforce full separation of the retail operations of UK banks to which the reforms apply under certain circumstances; and
- the FPC has direction powers over sectoral capital requirements and legal powers to make recommendations to the PRA and FCA which can direct capital changes (including raising capital requirements above microprudential standards on exposures to specific sectors such as commercial or residential property) in response to macroeconomic conditions.

- in common with other regulated UK deposit takers, the Bank is responsible for contributing to compensation schemes such as the FSCS in respect of banks and other authorised financial services firms that are unable to meet their obligations to customers. The compensation paid out to customers is currently funded through loans from HM Treasury. The Bank will be liable to pay a proportion of the outstanding borrowings that the FSCS has borrowed from HM Treasury. Additionally, the Bank is obliged to pay its share of management expenses and compensation based on the Bank's proportion of the total market protected deposits as at 31 December of each year. The term of these loans was interest only for the first three years with the FSCS recovering the interest cost, together with its own management expenses, through annual management levies on its members. By virtue of the Bank holding deposits under the FSCS scheme, the Bank has an obligation to pay levies in respect of the interest cost for 2014/2015. The Bank has provided £12.7 million as at 31 December 2014 (2013 restated: £13.3 million) for its share of the levies raised by the FSCS.

  Further provisions in respect of these costs are likely to be necessary in the future. The ultimate cost to the industry, which will also include the cost of any compensation payments made by the FSCS and, if necessary, the cost of meeting any shortfall after recoveries on the borrowings entered into by the FSCS, remains uncertain but may be significant and may have a material effect on the Bank's business, results of operations and financial condition

- *Measures at EU level*

  - the European Directive 2014/59/EU on Bank Recovery and Resolution ("**BRRD**"), which provides an EU-wide framework for the recovery and resolution of credit institutions and investment firms. It was adopted in June 2014, with an implementation deadline of 1 January 2015, save for the provisions in respect of the bail-in tool, which are to apply from 1 January 2016 at the latest. The BRRD is designed to provide relevant authorities with a set of tools to intervene sufficiently early and quickly in an unsound or failing institution so as to ensure the continuity of the institution's critical financial and economic functions, while minimising the impact of an institution's failure on the economy and financial system. In the United Kingdom, some of the requirements of the BRRD were already reflected in national law in the Banking Act. In addition, the Banking Act was amended to conform to the additional requirements in the BRRD, including the introduction of the bail-in tool as of 1 January 2015; however, the implementation of the minimum requirement for own funds and eligible liabilities ("**MREL**") regime has been deferred. The PRA has also published rules pursuant to the BRRD and the Banking Act which require the inclusion of a contractual clause recognising the bail-in powers in the respect of liabilities governed by the law of a non-EEA state. These rules became effective on 19 February 2015 in respect of debt instruments (including the Notes) and will apply to all other relevant liabilities from 1 January 2016. See also "*Risks relating to the Notes – The Bank is subject to the UK Banking Act. The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK banks and certain of their affiliates in the event a bank in the same group is considered to be failing or likely to fail. Furthermore, such actions can be taken directly against any relevant entity or against certain of its UK group companies. The exercise of any of these actions in*

relation to the Bank could materially adversely affect the value of the Notes, or could result in the principal amount of the Notes being written down or written off entirely" below.

- the European Commission proposals of January 2014 for a directive to implement recommendations of the Liikanen Review would apply to EU globally significant financial institutions and envisages, amongst other things: (i) a ban on engaging in proprietary trading in financial instruments and commodities; (ii) giving supervisors the power and, in certain instances, the obligation to require the transfer of other trading activities deemed to be 'high risk' to separate legal trading entities within a banking group; and (iii) rules governing the economic, legal, governance and operational links between the separated trading entity and the rest of the banking group.

- a number of other EU proposals are also currently going through consultation and legislative processes and will create new, amend or update existing Directives and Regulations. These include: the new Mortgage Credit Directive, which was adopted in February 2014 and must be implemented in the UK by March 2016; a new Payment Accounts Directive, which was adopted on 15 April 2014; revisions to the Payment Services Directive; a fourth Money Laundering Directive and a new Wire Transfer Regulation; revisions to the Deposit Guarantee Schemes Directive (2014/49/EU) ("**DGSD**"); and revisions to the Insurance Mediation Directive. MiFID II and a new associated Regulation MiFIR were adopted by the European Parliament on 15 April 2014.

It is not possible to predict with any certainty the effect that any of the proposed changes listed above will have on the Bank or how any of the proposals discussed above will be implemented in light of the fundamental changes to the regulatory environment proposed by the Government. Depending on the specific nature of the requirements and how they are enforced, such changes could have a material adverse effect on the Bank's business, balance sheet composition, operations, profitability, financial condition, structure, strategy, costs and/or capital requirements.

For further information on regulatory, legal and conduct related risks that the Bank is or may become exposed to, please refer to the risk factor "*The Bank is exposed to a number of conduct risks*".

An inability of the Bank to deleverage its Non-core Assets in an accelerated and capital efficient manner may have a negative impact on the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements. Any greater than expected costs or delays in deleveraging the Non-core Assets may divert funding from and adversely impact the growth of the Core Business. A number of the Non-core Asset classes have a small number of borrowers accounting for a large proportion of the total loans outstanding

The Bank's Non-core Assets consist of asset classes of the Bank which are not consistent with the Bank's Core Business strategy. As at 31 December 2014, the Non-core Business had total segment assets of £10,753.0 million, constituting 27.28 per cent. of the Bank's total assets and 62.2 per cent of the Bank's credit risk risk-weighted assets. The Bank's Non-core Assets therefore constitute a significant part of the Bank's total assets and a majority of its risk weighted assets.

A key part of the Bank's overall strategy is a run-off and exit of the Non-core Assets in an accelerated manner that seeks to ensure that the anticipated future losses from such run off and exit do not materially exceed the capital which is released from the reduction in risk weighted assets (including the reduction of risk weighted assets where stress tests are applied), and which the Directors believe minimises any adverse impact on the realisation of the Bank's Core Business strategy and the Bank's core customers. As part of this process, the Bank has reviewed its corporate loan book on an asset by asset basis, identified Non-core Assets for run-off and exit and changed the work out approach on a significant number of such assets. As part of its revised business plan, the Bank is seeking to accelerate the de-leverage on its Non-Core residential mortgage portfolio, Optimum. On 6 May 2015, the Bank successfully closed its inaugural whole capital structure securitisation of approximately £1.5 billion comprising part of its Non-Core residential mortgage portfolio, Optimum through Warwick Finance One. The pricing of future transactions would be dependent on the conditions in the securitisation markets or the 'whole loan' sale market.

A failure by the Bank to deleverage its Non-core Assets in accordance with its strategy may negatively impact on the Bank's business, operating results, financial condition (including its net interest margin) and prospects as well as its ability to comply with its regulatory capital requirements. It may also restrict the longer term development of the Core Business' business and divert management attention from the Core Business. The Non-core Business is partially funded by retail deposits from the Core Business. Any unanticipated costs or delays in the exiting and running down of the Non-core Assets may require additional funding from the Core Business and adversely impact the growth of the Core Business. In addition, given the period over which the Bank will be running off and exiting from its Non-core Assets, the Bank is exposed to market conditions, including declines in commercial property values, and other macro-economic factors.

The Non-core Business' corporate asset book is relatively concentrated, with the result that a small number of borrowers account for a large proportion of the total loans outstanding. Any significant additional impairment of any of these borrowers would result in a disproportionate impact on the Bank's operating results and financial condition. The strategies on these connections are however reviewed on a regular basis to ensure impairment levels remain appropriate.

The Bank holds certain securities in and owes obligations under the Warwick Finance One securitisation transaction. There is a risk that this may have a material adverse effect on the Bank's business, operating results, financial condition, prospects and its ability to achieve its strategy

On 6 May 2015, the Bank successfully closed its inaugural whole capital structure securitisation transaction of approximately £1.5 billion comprising part of its non-core residential mortgage portfolio, Optimum, through Warwick Finance One.

The Bank purchased 65 per cent. of the class A notes (being a principal amount of £707,200,000) issued by Warwick Finance One in order to manage its liquidity position. Accordingly, the Bank retains the liquidity, credit and market risks in relation to its holding of the class A notes until such time as the class A notes are sold by the Bank in the secondary market. Such risks may have a material adverse effect on the market value of the class A notes and thus the price at which the securities may be sold in the open market. A change in the market value of the class A notes may give rise to a mark to market impact and a change in the Bank's reserves. If the class A notes are subsequently downgraded by a rating agency, the Bank may be required to increase the regulatory capital requirement that the Bank currently holds for the class A notes. Any reduction in the value of the class A notes may have a material adverse effect on the Bank's business, operating results, financial conditions, prospects and its ability to achieve its strategy.

Further, the Sellers have, in accordance with Article 405 paragraph (1) of the CRR and amending Regulation (EU) No 648/2012, Article 51 of Regulation (EU) No 231/2013, referred to as the Alternative Investment Fund Managers Directive ("**AIFMR**"), and Article 254(2) of the Commission Delegated Regulation (EU) 2015/35 of 10 October 2014 supplementing Directive 2009/138/EC of the European Parliament and of the Council on the taking-up and pursuit of the business of Insurance and Reinsurance (Solvency II) (the "**Solvency II Delegated Act**"), to the extent the regulations above continue to apply and in each case as they are interpreted and applied on the closing date (and in the case of AIFMR taking into account Article 56 of the AIFMR), retained a net economic interest of at least 5 per cent. of the nominal value of the securitised exposures sold by the Sellers to Warwick Finance One for the purposes of the securitisation transaction. At closing, the interest comprised not less than 5 per cent. of randomly selected exposures which would otherwise have been securitised by the relevant Seller in the transaction effected by Warwick Finance One.

The Basel III reform package implemented into the EEA through CRD IV establishes a single set of harmonised prudential rules which apply directly to all credit institutions in the EEA. In connection therewith, the Basel Committee has also published certain proposed revisions to the securitisation framework, including changes to the approaches to calculating risk weights and a new risk weight floor of 20 per cent. If implemented in the UK, such changes may have an impact on the capital requirements in respect of the class A notes held by the Bank and as a result have a material adverse effect on the Bank's business, operating results, financial conditions, prospects and its ability to achieve its strategy.

The Bank has provided a guarantee to Warwick Finance One in respect of (i) the mortgage loan repurchase obligations of the indirect subsidiaries of the Bank that sold mortgage loans to Warwick Finance One (the "**Sellers**") under the mortgage sale agreements (entered into between the Sellers and Warwick Finance One) for breach of representation and warranty in relation to the mortgage loan assets

sold to Warwick Finance One that would cause a material adverse effect on the value of the loan; and (ii) the conduct risk remediation payments to be made by Sellers to affected borrowers in the Warwick Finance One portfolio (through loan write-down) in the event that the balance of the conduct reserve ledger of £4.92 million (as funded at closing) to compensate Warwick Finance One for such loan write-downs is insufficient to fund the remaining costs associated with the write-downs of the loans and the Sellers are unable to meet such further costs. If the Sellers are not in a financial position to meet their obligations, the Bank will meet these obligations through the guarantee. There is a risk that claims under such guarantees may have a material adverse effect on the Bank's business, operating results, financial conditions, prospects and its ability to achieve its strategy.

The Bank faces competition in all of the core markets in which it operates. There is a risk that the Bank may lose market share to its competition and this could have a material adverse effect on the Bank's business, operating results, financial condition and prospects

Competition in the UK personal financial services market may adversely affect the Bank's operations. The Bank competes mainly with other providers of personal financial services, including other banks, building societies and insurance companies, and operates in an increasingly competitive UK personal financial services market. Each of the main personal financial services markets in which the Bank operates is mature and slow-growing, so that growth requires taking market share from competitors.

The Competition and Markets Authority (the "**CMA**") announced in November 2014 its decision to launch an in-depth market investigation review into the personal current account and SME retail banking sectors, confirming its provisional decision of 18 July 2014. Together with other significant retail and SME banks in the UK, the Bank is required to participate in the investigation which is being conducted by a Market Reference Group drawn from the CMA's panel of independent members. The CMA is scheduled to publish its final report and recommendations in April 2016 and until such time the impact to the Bank and the wider industry as a whole is unknown and yet to be determined.

Competition could result in the Bank losing existing and potential new customers in a number of situations, particularly where:

- the Bank is not successful in strengthening its core proposition and brand positioning with retail and SME customers;
- the Bank is unable to match its competitors for example, in the quality of its products and the provision of additional services such as mobile banking, and in keeping up with consumer demand and technological changes;
- if the Bank's customer service levels were perceived to be negatively impacted by the implementation of its strategy, or were perceived by the market to be only in line with, or materially below, those of competitor UK financial institutions;
- reputational risk arises in respect of the Bank;
- a loss of customers, or deteriorating customer relationships, as a result of these or other factors, could result in the Bank losing liability/asset balances to competitors, which may in turn have an adverse effect on revenue. This could materially adversely affect the Bank's business operating results, financial condition and prospects;
- there remains significant competition for market share across the Retail product lines, and there is a risk that failure to develop the core proposition and other differentiating factors will result in growth plans reliant on pricing to win market share, which will impact margins;
- there is a risk that levels of marketing investment (required to grow customer awareness and consideration) are insufficient due to the levels of similar investment from the competition. Since the introduction of the Current Account Switching Service, the Bank has experienced a period of significant incremental advertising spend by its competitors and sustained negative newsflow about the Bank, the combination of which has contributed to an increase in the number of accounts switching from the Bank. A net 66,345 current accounts were lost during 2014 (accounting for less than 4.5 per cent. of the opening stock of accounts). Any failure to attract new, or retain old customers or to maintain the Bank's market share may result in the loss of the

Bank's asset and liabilities balance to its competitors, which may in turn impact the Bank's ability to deliver its turnaround plan. See the risk factor entitled "*Reputational risk could cause harm to the Bank, its business, operating results, financial condition and prospects and question the Bank's commitment to co-operative values and ethics*" for further information; or

- risk of competition from a new bank competitor.

The Bank's business is subject to inherent risks concerning liquidity, particularly if the availability of traditional sources of funding such as retail deposits becomes limited and/or becomes more expensive, and this may have an adverse effect on the Bank's business, profitability and ability to meet its liabilities as they fall due

The Bank is subject to liquidity risk as an inherent part of its business. Liquidity risk is the risk that an institution may not have sufficient funds at any point in time to make full payment in respect of liabilities falling due, or can only do so at excessive cost. This may result in an inability to operate in the ordinary course and/or a failure to meet liquidity or regulatory capital requirements, and/or may adversely impact the Bank's business and/or the implementation of its strategy.

The Bank raises the majority of its funding through accepting retail and commercial deposits. The Bank also maintains a range of funding programmes (including medium-term note, securitisation and covered bond programmes) targeting wholesale investors.

Given the reliance by the Bank on its customer deposits to provide funding, any severe decline in customer confidence in the Bank could increase the amount of deposit withdrawals in a short space of time or over a sustained period. Should the Bank experience an unusually high level of withdrawals which exceed the Bank's ability to manage its liquidity, this may have an adverse effect on the Bank's day-to-day operations, and its ability to maintain the Bank's planned lending. This in turn may have an adverse effect on the Bank's business, operating results and financial condition and could, in extreme circumstances, prevent the Bank from meeting its financial obligations as they fall due, meeting its regulatory minimum liquidity requirements or fulfilling its commitments to lend. In such circumstances, the PRA may exercise any of its wide-ranging powers over the Bank, including imposing a resolution procedure under the Banking Act.

As part of the Bank’s revised business plan it expects to reduce the level of its customer deposit balances. There is a risk that the pricing reductions implemented to achieve this may create unanticipated levels of customer deposit reductions. In addition, there is a risk that unanticipated levels of customer deposit reduction may be triggered by other proposed actions in the Bank’s revised business plan such as branch closures and savings backbook simplification.

As part of the Bank’s deleveraging of its Non-core Assets, it expects to reduce its funding requirement through a combination of asset sales, run off and managed repayments, net of new drawdowns. Any delay in the deleveraging process may increase liquidity pressures on the Bank.

In connection with the Bank's securitisation and covered bond programmes, the Bank makes various representations and warranties relating to the mortgage loans sold to the programmes. If the representations and warranties are breached, the Bank may in some circumstances be required to repurchase the affected mortgage loans or pay compensation to the relevant special purpose vehicle.

The accelerated repayment of the securitisations and/or the mandatory sale of further loans to the covered bond programme as a result of a breach of the aforementioned representations and warranties could reduce the Bank's primary liquidity and could also impact secondary liquidity. Furthermore, the early repayment of securitisations will also reduce funding balances and primary liquidity balances.

The Bank's ability to access retail and wholesale funding sources on satisfactory economic terms or at all is subject to a variety of factors, some of which are outside the control of the Bank. Factors which apply generally include; general economic conditions (including interest rates) and market volatility, market dislocation, confidence in the UK banking system and the economy in general and the financial services industry specifically, regulatory requirements and major disasters.

Rating downgrades and/or negative market sentiment with respect to the Bank, the sector and/or the UK may have an adverse effect on the Bank's performance

The Bank's ratings have been adversely affected by concerns regarding the Bank's capital position. The Bank's debt does not currently have an investment grade rating. The Bank is rated:

- B (long-term and outlook negative) and B (short-term) by Fitch; and
- Caa2 (long-term senior unsecured rating under review for possible downgrade) and NP (short-term) by Moody's.

On 16 March 2015, Moody's published its updated bank rating methodology. On 17 March 2015, Moody's placed the following ratings of the Bank under review:

- long-term deposit rating of Caa2 on review for possible upgrade:
- baseline credit assessment of ca on review for possible upgrade;
- adjusted baseline credit assessment of ca on review for possible upgrade; and
- long term senior unsecured rating of Caa2 on review for possible downgrade.

The Bank cannot be certain as to the ratings outcomes of the Moody's review of the Bank's ratings under Moody's new methodology.

The Bank raises the majority of its funding through accepting retail and corporate deposits. The Bank also has issued funding from a range of programmes (including medium-term note, securitisation and covered bond programmes) targeting wholesale investors.

In 2013, Fitch and Moody’s downgraded the Bank’s senior debt ratings from investment grade to sub-investment grade. The 2013 credit rating downgrades have:

- led to sub-investment grade ratings on the Bank's senior debt leading to a significant reduction in the demand for these types of instruments and ratings sensitive customer deposits;
- negatively impacted the Bank's ability to access short-term unsecured wholesale funding; and
- increased the Bank's collateral requirements used in the clearing and payment systems.

The credit rating downgrades in 2013 have affected the Bank's funding profile and the cost to the Bank of raising new funding. The impact on access to funding and increased cost of funding may therefore, over the longer term, have an adverse effect on the Bank's business, operating results, financial condition and/or prospects and/or adversely affect the Bank's ability to achieve its strategy.

Any downgrade of the UK sovereign credit rating or the perception that such a downgrade may occur could destabilise the markets, impact the Bank's own rating and borrowing costs and have a material adverse effect on the Bank's operating results and financial condition.

The Bank could be negatively affected by a deterioration or a perceived deterioration in the soundness of other financial institutions and counterparties

There is a high level of interdependence between financial institutions as a result of their credit, trading, clearing and other relationships. The Bank routinely executes a large number of transactions with counterparties in the financial services industry, resulting in large daily settlement amounts and significant credit exposure. As a result, the Bank is and will continue to be subject to the risk of deterioration of the commercial and financial soundness, or perceived soundness, of other financial services institutions. Within the financial services industry, the default of any one institution could lead to defaults by other institutions. Concerns about, or a default by, one institution could lead to significant liquidity problems, losses or defaults by other institutions. Even the perceived lack of creditworthiness of, or questions about, a counterparty may lead to market-wide liquidity problems and losses or defaults by the Bank or by other institutions. This systemic risk could have a material adverse effect on the Bank's

ability to raise new funding and on its business, financial condition, results in operations, liquidity and/or prospects.

The Bank is under intense regulatory scrutiny and expects that environment to continue. The Bank is also the subject of multiple regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them and may also be subject to other legal and/or regulatory proceedings

As a financial services firm, the Bank is subject to extensive and comprehensive regulation under the laws of the jurisdictions in which it does business. These laws and regulations significantly affect the way that the Bank does business, and can restrict the scope of its existing businesses and limit its ability to expand its product offerings, or can make its products and services more expensive for clients and customers. There has also been an increased focus on regulation and procedures for the protection of customers and clients of financial services firms. This has resulted in increased willingness on the part of regulators to investigate past practices of financial services firms both on an industry-wide basis and focusing on particular firms.

The Bank is exposed to many forms of legal and regulatory risks, including that:

- business may not be, or may not have been, conducted in accordance with applicable laws and regulations and financial and other penalties may result, as well as potential liabilities to customers by way of redress for prior breaches;
- contractual obligations may either not operate or be enforceable as intended or may be enforced in a way adverse to the Bank;
- the Bank's assets such as intellectual property may not be adequately protected and the Bank may use intellectual property which infringes, or is alleged to infringe, the rights of third parties; and
- litigation by or against the Bank is not appropriately managed to protect the Bank's reputation and achieve the best outcome and that liability for damages may be incurred to third parties harmed by the conduct of the Bank's business.

The Bank is subject to or involved in several on-going regulatory investigations and enquiries, including by (but not limited to):

- the PRA, which is undertaking an enforcement investigation in relation to the Bank and as part of that investigation will consider the role of former senior managers;
- the FCA, which is undertaking enforcement investigations covering decisions, events and processes at the Bank over the period from the Merger with Britannia (each as defined in paragraph 1 (*Overview*) of the section entitled "*Description of the Bank*") to the end of 2013. These enforcement investigations carried out by the FCA and PRA began in January 2014 and have now been ongoing for 18 months. FCA and PRA have recently indicated that their preliminary view is that they are minded to make findings against the Bank covering certain decisions, events and processes over the period from mid-2008 to end 2013. Based on their current view, the FCA and PRA have indicated they intend to commence formal settlement discussions in July 2015. The outcome of any settlement discussions is currently uncertain both in the details of any findings and any potential financial penalty. No indication of the potential quantum of any financial penalty contemplated by FCA and PRA has yet been given to the Bank;
- HM Treasury, first announced in November 2013 and confirmed in March 2015 (following the publication of the Treasury Select Committee report into the Bank) that it would appoint a skilled person to review events at the Bank and the circumstances surrounding them from 2008, including the Verde transaction (being the bid to purchase the separated part of the Lloyds Banking Group's retail business, the "**Verde transaction**") and the Merger with Britannia. The investigation will review the actions of relevant authorities (regulators and government) but will not commence until it is clear that it will not prejudice the outcome of the PRA and FCA investigations mentioned above; and

- the Financial Reporting Council (the "**FRC**"), which launched an investigation under its Accountancy Scheme into the preparation, approval and audit of the Bank's accounts over the financial years 2009 – 2012. The focus of the FRC investigation is into the role of auditors or individual accountants rather than the Bank itself.

The outcome of these enquiries or any other existing, potential or future legal, regulatory or other enquiries, investigations or proceedings, is difficult to predict, but regardless of their ultimate outcome, they will involve the Bank incurring significant expense. Consequently, the Bank could be exposed to: substantial monetary damages and fines, other penalties and injunctive relief, potential for additional civil or private litigation, potential for criminal prosecution in certain circumstances, potential regulatory restrictions on the Bank's business, greater scrutiny and/or investigation from regulators and/or regulatory or legislative actions, and/or a negative effect on the Bank's reputation and its brand and its ability to recruit and retain personnel and customers. Any of these risks, should they materialise, could have an adverse impact on the Bank's business, operating results, financial condition and prospects, its regulatory capital position or its ability to comply with regulatory capital requirements, as well as taking up a significant amount of management time and resources.

Any adverse findings of these investigations may, therefore, reduce, directly or indirectly, the attractiveness of the Bank to stakeholders and may lead to customer attrition, reduced workforce morale and difficulties in recruiting and retaining talent. Sustained damage arising from any adverse findings could, therefore, lead to loss of revenue for the Bank and could have a materially negative impact on the Bank's business, operating results, financial condition and prospects.

See the risk factors entitled "*Reputational risk could cause harm to the Bank, its business, operating results, financial condition and prospects and question the Bank's co-operative values and ethics*", "*The Bank is currently involved in litigation and may in the future become involved in further litigation. The outcome of any legal proceedings is difficult to predict", "A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*" and "*The Bank is exposed to a number of conduct risks*" for further information.

The Bank is currently involved in litigation and may in the future become involved in further litigation. The outcome of any legal proceedings is difficult to predict

The Bank is engaged in various legal proceedings in the United Kingdom, involving claims both by and against it, which arise in the ordinary course of business, including (but not limited to) debt collection, mortgage enforcement, consumer claims and contractual disputes. Whilst the Bank does not expect the ultimate resolution of any of these known legal proceedings to which the Bank is party to have a material adverse effect on the results of operations, cash flows or its financial position, and whilst provisions have been recognised for those cases where the Bank is able reliably to estimate the probable loss where the probable loss is not de minimis, the outcome of litigation is difficult to predict and there can be no assurance that such provisions will be sufficient to cover the costs associated with such litigation. The outcome of any such litigation could adversely impact the Bank's reputation and brand, could result in additional similar claims being brought and/or, if perceived as a systemic or pervasive conduct issue, could result in further investigations or enquiries by the Bank's regulators. The costs of pursuing or defending legal proceedings, and the outcome of any such proceedings, could have a material adverse impact of the financial condition of the Bank.

Reputational risk could cause harm to the Bank, its business, operating results, financial condition and prospects and question the Bank's commitment to co-operative values and ethics

The Bank's reputation is one of its most important assets. Its ability to attract and retain customers and deposits and to conduct business with its counterparties could be adversely affected to the extent that its reputation or its brand is damaged. The act of addressing or failing to address, or appearing to fail to address, issues that could give rise to reputational risk is likely to cause harm to the Bank and its business prospects. The Bank's reputation could be impacted by both known issues and issues not yet identified (some of which could only have an ancillary connection to the Bank). For example, litigation, or the misconduct of employees or other persons (including criminal activity) at any time associated with the Co-operative brand or the "Co-operative Bank" brand, operational failures, accidents, the outcome of regulatory investigations, media speculation and negative publicity, breaches of data protection or other

laws, products considered to be inappropriate and sub-standard customer service, among other factors, could impact the Bank's reputation. Reputational damage could arise from, without limitation, any of the following (along with media speculation regarding the same where relevant):

- a requirement to raise further capital in the future, which could affect, or be perceived to affect, confidence in the Bank;
- a failure to implement the Bank's strategy and execute the Bank's revised business plan;
- a perception that the Bank has moved away from its co-operative values and ethics or there are breaches of the new Values & Ethics policy by the Bank or its employees;
- a reduction in the Bank's customer service levels resulting from cost cutting and outsourcing;
- a conflict between the mutual and ethical reputation of the Co-operative brand with the value maximisation objective of other shareholders of the Bank and the duties of the Bank's board of directors (the "**Board**") to such shareholders, and more generally, the Bank's association with the Co-operative brand, including any actions or omissions or speculation by or about the Co-operative Group. See the risk factor entitled "*The Bank will continue to rely on the Co-operative brand*" for further information;
- a conflict between the value maximisation objective of other shareholders of the Bank and the regulatory and prudential requirements of the regulatory authorities;
- the Bank ceasing to provide facilities for particular high profile customers as a result of its reconsideration of risk appetite and of its re-focusing on retail and SME customers;
- the risk that the Secretary of State for Business, Innovation and Skills may direct the Bank to change its registered name, or that the FCA or a third party may prevent the use of the "Co-operative" name, or take other action regarding the Bank's branding;
- matters relating to the Co-operative Group or its governance or to its current or former employees or management which adversely impact the Bank brand;
- adverse findings following from any legal or regulatory investigation into the Bank's conduct or investigations connected to the Bank; see the risk factor entitled "*The Bank is under intense regulatory scrutiny and expects that environment to continue. The Bank is also the subject of multiple regulatory and other investigations and enquiries into events at the Bank and circumstances surrounding them and may also be subject to other legal and/or regulatory proceedings*" for a list of investigations.
- failing to appropriately address potential conflicts of interest;
- breaching or facing allegations of having breached legal and regulatory requirements and a subsequent enforcement action or regulatory investigation;
- failing or facing allegations of having failed to maintain appropriate standards of customer privacy, customer service and record keeping;
- technology failures that impact upon customer services and accounts;
- internal fraud;
- failing to properly identify legal, reputational, credit, liquidity and market risks inherent in products offered;
- the change to the Bank's auditors; and
- generally poor Bank performance or customer service.

A failure to address these or any other relevant issues appropriately could make significant numbers of customers, depositors and investors unwilling to do business with the Bank. For example, if the negative

newsflow continues for a significant period of time, there is the risk that the Bank will lose a material number of customers and liability/asset balances to competitors. This could materially adversely affect the Bank's business, operating results, financial condition and prospects and could damage its relationships with its regulators. The Bank cannot ensure that it will be successful in avoiding damage to its business from reputational risk.

The Bank is exposed to a number of conduct risks

The Bank is exposed to many forms of legal and regulatory risk. A number of conduct-related issues, as disclosed below, have been identified as a result of both internal and external reviews. The Bank is seeking to remediate and redress such matters and has commenced redress programmes for these issues.

As part of its strategy to identify and resolve outstanding liability issues, the Bank has commenced a structured risk based product review process, which may result in the discovery of further conduct-related issues.

It is recognised that whilst progress has been made in identifying conduct issues, no assurance can be given that further issues or breaches will not be identified. Examples of legal and regulatory risk potentially faced by the Bank include:

Legal and regulatory supervision and scrutiny

- Given the high level of scrutiny regarding financial institutions' treatment of customers and business conduct from regulatory bodies, there is a risk that aspects of the Bank's current or historic business may be determined by the PRA, the FCA, HM Treasury, the Financial Ombudsman Service, the OFT, or other regulatory bodies or the courts as not being conducted in accordance with applicable laws or regulations (or in the case of the Financial Ombudsman Service, in accordance with what is fair and reasonable in the opinion of the Financial Ombudsman). If the Bank fails to comply with any relevant regulations, there is a risk of an adverse impact on its business due to sanctions, fines or other actions imposed by the regulatory authorities. There is also a risk of greater scrutiny and/or intervention from regulators, further regulatory action and/or litigation. The nature of any future disputes and legal, regulatory or other investigations or proceedings into such matters cannot be predicted in advance. Furthermore, the outcome of any ongoing disputes and legal, regulatory or other investigations or proceedings is difficult to predict. This would take a significant amount of management time and resources away from management of the Bank's business. In addition, such action could lead to substantial monetary damages and/or fines, public reprimands, a negative effect on the Bank's reputation or potential regulatory restrictions on the Bank's business. Any of these risks, should they materialise, could have an adverse impact on the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with regulatory capital requirements.

Mis-selling and unauthorised transactions

- There are a number of areas where the Bank has or may sustain financial and reputational damage due to conduct related matters and where consequences are likely to endure. These include matters relating to (amongst others) (i) the alleged mis-selling of financial products (including payment protection insurance ("**PPI**"), including as a result of having sales practices and/ or reward structures in place that are determined to have been inappropriate; (ii) alleged failings relating to the introduction of third party sales of card and identity protection and other products; (iii) arrears fees and associated charges; (iv) early repayment charges ("**ERC**"); (v) the processing of first payments on certain mortgages; (vi) the mis-selling of interest rate swaps; (vii) the miscalculation of interest on corporate loans; (viii) unauthorised transactions with customers; and (ix) the alleged mis-selling of packaged current accounts (see next paragraph for further information). A provision raised in the Bank's 2014 financial statements is based on the FSA's (as it was then known) policy statement and industry claims experience, and on the published views and requirements of the FCA (which, for the avoidance of doubt, are not specific to the Bank). Any change in the FCA's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, could have a material adverse impact on the financial condition of the Bank and there is a risk of greater scrutiny and/or further regulatory action from the FCA. Such conduct related matters may have an adverse effect on the Bank,

including (i) disciplinary action (including significant fines); (ii) requirements to amend sales processes, withdraw products or provide restitution to affected customers; and (iii) an adverse impact on future revenues from affected products. Whilst the Bank's provision for customer redress is reflected in a significant item charge, there can be no assurance that its estimates for potential liability are correct and the Bank's provisions taken to date might prove inadequate.

- In November 2014, the Supreme Court handed down a decision in Plevin v Paragon Personal Finance Ltd [2014] UKSC 61. The decision concerns the disclosure of commission amounts received in respect of sales of single premium PPI. In line with the rest of the banking industry and the Financial Ombudsman Service, the Bank is considering the implications of the judgement on both current and prior claims made concerning both single and repeat premium PPI. The decision has a potential impact on the number of the Bank's customers who may have a claim for PPI mis-selling and the treatment of prior claims. However, the Bank is not currently able to determine if it will need to make additional provisions in relation to the judgement. There is a risk, depending on the interpretation and application of the judgement that the Bank, in line with the banking industry in general, may need to make additional provisions for PPI. While the Bank continues to review the position, the decision is also most relevant to CCA regulated loans.

Packaged current accounts

- The risks associated with the potential mis-sale of packaged current accounts are an industry-wide issue. There is increased scrutiny by regulatory bodies and there is a risk of increased numbers of complaints from customers and through claims management companies. The Bank has identified a limited number of issues relating to certain product features and groups of customers where it has concluded that redress is appropriate. As at 31 December 2014, a provision of £17.4 million was raised (2013: £0). The Bank continues to keep the wider position under review and there is a risk that further deficiencies may be identified. The Bank's approach to provisions for historic mis-selling of packaged current accounts is based on the views and requirements of the FCA. Any change in the FCA's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, could have a material adverse impact on the financial condition of the Bank and there is a risk of greater scrutiny and/or further regulatory action from the FCA.

Mortgages

- Regulatory scrutiny with respect to mortgages has increased, for example in respect of forbearance, and issues relating to irregularities in mortgage documentation. There is a risk that past forbearance may have given rise to customer detriment. The Bank has undertaken a review of its compliance with the FCA's Mortgages and Home Finance Code of Conduct sourcebook ("**MCOB**"), including in the Bank's mortgage origination, administration and arrears processes, and the Bank is now implementing changes to ensure compliance. Should the Bank not comply with MCOB requirements in relation to mortgage selling in the future, absent FCA forbearance, it could be required to cease this activity until such time that it can demonstrate compliance with the relevant rules and guidance.

- The Bank has identified defects in certain of its historic mortgage documentation which raise legal and conduct risks, including potentially rendering certain previously mortgage related fees and charges not payable by the customer. A provision relating to additional costs arising from such defects was initially raised in 2013. As of 31 December 2014, a provision of £7 million was raised. There is a risk that such provisioning may prove inadequate if the actual costs of remediation and redress and any additional costs of enforcing affected mortgages, are higher than currently estimated or that the assessment of the impact of such defects proves to be incorrect or incomplete.

- The Bank, in selling regulated mortgages must adhere to specific guidelines, principles and regulations. The Bank is also in the process of outsourcing its mortgage system and servicing operations. There are instances where the sales of these products have fallen short of the required standard and include issues relating to ERC, arrears fees, product charges and interest charges which create a risk that the Bank could be subject to enforcement action by the FCA/PRA. The Bank may have difficulty in complying with the FCA requirements in relation to mortgage selling in the future, and may be required to cease selling regulated mortgages until

such time as the Bank can demonstrate compliance. An inability to sell mortgage products would have a material adverse effect on the Bank's business, operating results, financial condition and prospects. Mortgages are a significant part of the Bank's Core Business and any restriction on this activity could, for example, impact the Bank's liquidity and its securitisation programmes.

- The Bank remains under close regulatory scrutiny in respect of mortgage arrears handling where there is a risk of sanction penalty and possible additional redress.

*Consumer Credit Act 1974 ("**CCA**")*

- There has been a focus on the CCA which regulates consumer lending and governs the way in which banks provide consumer credit to certain customers. In the event that the highly technical requirements of the CCA are not precisely complied with, the Bank is exposed to the risk that its agreements with customers are not enforceable without the benefit of a court order and/or that during a period of non-compliance the Bank's customer is not liable to pay interest or default charges. The Bank has identified that it has breached certain provisions of the CCA and may therefore be subject to these risks. Provisions have been made in the 2013 and 2014 financial statements in respect of the costs associated with such breaches but there is a risk that these may be inadequate. Certain of the identified breaches are failures to comply with section 77A of the CCA, which requires the Bank to send its customers statements which comply with particular requirements. Having sent statements which fail to comply with section 77A, the Bank must refund all interest and charges paid by customers during the period of non-compliance. Similarly, the Bank has identified breaches of section 86B of the CCA, which requires the Bank to send customers Notice of Sums in Arrears ("**NoSIAs**") at specific intervals and which comply with particular requirements. Having sent NoSIAs which fail to comply with section 86B, the Bank must refund all interest and charges paid by customers during the period of non-compliance.

- The Bank was notified on or about 16 April 2014 by its third party credit card servicer of a deficiency in their processing of NoSIAs under section 86C of the CCA, which they had identified affected a number of their financial services clients. If the indications provided by the third party servicer are correct the issue would not have a material impact on the Bank's financial position. However, in the event that the third party supplier's information and estimates are incorrect and the defects are broader in scope or duration, there could be a greater financial impact on the Bank. The Bank has conducted a full review of its third party credit card servicer in relation to CCA and it has not identified any significant issues which would impact the Bank's financial position.

- The Bank continues to review its CCA related products and therefore there remains a risk that further issues may emerge.

Money laundering, bribery and terrorist financing

- Failure by the Bank to implement and maintain adequate policies, procedures and controls to combat money laundering, bribery and terrorist financing or to ensure economic sanction compliance could have serious legal and reputational consequences, including exposure to fines, public censure, penalties and damages. The Bank has identified a number of significant control weaknesses and there may be instances in which UK and European law obligations with respect to anti-money laundering and terrorist financing controls may not have been met. See the risk factor entitled "*Anti- money laundering, anti-bribery, sanctions and other compliance risks*" for further information.

Failure to appropriately manage conduct and reputation risks could lead to significant liabilities or reputational damage, reduce (directly or indirectly) the attractiveness of the Bank to stakeholders, including customers, and may lead to negative publicity, loss of revenue, litigation, higher scrutiny and/or intervention from regulators, regulatory or legislative action, loss of existing or potential client business, reduced workforce morale, and difficulties in recruiting and retaining talent. Sustained damage arising from conduct and reputation risks could have a materially negative impact on the Bank's business, operating results, financial condition and prospects, its regulatory capital position, its ability to comply with regulatory capital requirements and customer relations.

Anti-money laundering, anti-bribery, sanctions and other compliance risks

Combating money laundering, bribery and terrorist financing and compliance with economic sanctions has been a major focus of government policy relating to financial institutions in recent years (most notably in the UK and the EU). UK and EU law and regulations impose obligations on the Bank to maintain appropriate policies, procedures and controls to detect, prevent and report money laundering and terrorist financing. Failure by the Bank to implement and maintain adequate policies, procedures and controls to combat money laundering, bribery and terrorist financing or to ensure economic sanction compliance could have serious legal and reputational consequences for the institution, including exposure to fines, public censure, penalties and damages. The Bank has identified a number of significant control weaknesses with respect to its anti-money laundering, sanctions and terrorist financing controls and there may be instances in which obligations imposed by UK and EU law with respect to anti-money laundering, sanctions and terrorist financing controls have not been met. There is a risk of the FCA exercising its powers over the Bank (including imposing fines) in respect of such control weaknesses. However, the Bank has discussed these shortcomings with the FCA and has provided a commitment to the FCA to strengthen its anti-money laundering, sanctions and terrorist financing controls.

The Bank's policies and processes for risk management may prove inadequate for the risks faced by its business. Any failure to properly manage the risks which it faces could cause harm to the Bank and its business prospects

Managing Risks

The Bank's risk-management framework ("**RMF**") has been weak and there have been failings in a number of areas in the past. To address this, the foundation of a more robust RMF has been laid. However, further time and significant work is required to embed all elements of the RMF across the Bank. This may lead to the identification of further risks and control failings which could potentially impact the business, operating results, financial condition and prospects of the Bank.

The Bank's RMF divides its "business as usual" risks into areas such as credit risk, liquidity risk, market risk and operational risk:

Credit Risk

Credit risk is an inherent part of the business activities of the Bank (and all other banks). It is inherent in both traditional banking products (loans, mortgages and other credit products) and in "traded products" (derivative contracts such as forwards, swaps and options), repurchase agreements, securities borrowing and lending transactions. The risks arising from the general economic environment continue as a result of the prolonged period of significant turbulence and uncertainty affecting the global economy, financial systems and continued economic malaise. The Bank continues to be exposed to these risks and their consequences, including lower consumer confidence, high levels of unemployment, interest rate volatility and the increased cost of credit, which may result in increased credit risk and could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

Liquidity Risk

The Bank faces liquidity risk, particularly if the availability of traditional sources of funding such as retail deposits becomes limited and/or becomes more expensive. This may have an adverse effect on the Bank's business, profitability, financial condition and ability to meet its liabilities as they fall due. See the risk factor entitled "*The Bank's business is subject to inherent risks concerning liquidity, particularly if the availability of traditional sources of funding such as retail deposits becomes limited and/or becomes more expensive, and this may have an adverse effect on the Bank's business, profitability and ability to meet its liabilities as they fall due*" for further information.

Market Risk

The Bank risks losses arising as a result of the value of financial assets or liabilities (including off-balance sheet instruments) being adversely affected by movements in market rates or prices. The Bank's Treasury function also creates market risk through its various portfolio management and trading activities along with currency risk.

Changes in currency rates affect the value of assets and liabilities denominated in foreign currencies and may affect income from assets and liabilities denominated in foreign currency. The Bank also faces risks arising out of changes in interest rate levels, yield curves and spreads, which may affect the Bank's interest rate margin realised between lending and borrowing costs. The Bank seeks to minimise the volatility of future earnings from interest rate changes and all fixed interest rate risk exposure is removed from the Core Business and the Non-core Business and consolidated at the centre where it is managed from the core balance sheet within agreed limits. See the risk factors entitled "*The Bank's earnings and net interest margins have been adversely affected by a number of factors and may continue to be adversely affected for so long as one or more of these factors persist. In addition, regulatory capital shortfall and other recent events impacting the Bank may have an adverse effect on the Bank's net interest margin*" and "*Worsening economic and market conditions and/or increasing interest rates and/or a fall in housing prices could result in increased residential mortgage and unsecured loan losses which would adversely impact the Bank's financial and operational performance*" for further information.

Model Risk

The Bank uses models which are mathematical representations of business systems designed to help describe, predict, experiment with or optimise decisions and scenarios and are used throughout the Bank's business. There is a risk that adverse outcomes might occur as a result of weaknesses or failures in the design or use of a model. The Bank is required to make further investment, in model development to overcome existing shortcomings in a number of its models (including the Internal Ratings Based ("**IRB**") approach) and to ensure it can attest to compliance with CRR, support compliance with new accounting standards (IFRS9, as defined below in the risk factor entitled "*Changes in the Bank's accounting policies or in accounting standards could materially affect how it reports its financial condition and operating results*") and optimise customer decision-making through re-developed scorecards. Furthermore, in March 2015, the Bank was required to attest to the PRA its compliance with the CRR in relation to current IRB permissions. The Bank carried out a comprehensive assessment of its compliance with the requirements in delivering the required attestation. Areas of uncertainty remain with respect to ongoing data weaknesses and/or model performance such that the Bank is currently unable to complete an attestation to the satisfaction of the PRA. The Bank intends to supplement its attestation based on a further internal assessment in a time frame to be agreed with the PRA and which is intended to deliver a compliant process, at which point an assessment will be made as to its ongoing IRB permissions. There is a risk that as a result of the Bank's inability to make a compliant attestation, the Bank would need to consider adopting a standardised credit risk approach for residential mortgages. A consequence of adopting such an approach would be that the Bank may need to raise further capital or otherwise may result in the Bank failing to implement its revised business plan. Such risks could have a significant adverse effect on the Bank’s business, operating results, financial condition and/or prospects.

Changes to RWA floors

In the event that the PRA in line with some other European regulators implemented an increased level of risk weighted asset ("**RWA**") floor applicable to residential mortgage portfolios, there is a risk that the Bank’s capital and other ratios may be impacted as a result of such change and there is a further risk that the Bank may not meet its ICG and capital planning buffer requirements. Other European jurisdictions (including Sweden) have already implemented a 15 per cent. RWA floor and the FSA (as it was then known) previously used a residential mortgage floor as part of its calculations when assessing the amount of additional capital UK banks would have to raise pursuant to its announcement of 27 March 2013 entitled "Methodology note on calculating capital pressures". The Bank continues to monitor developments and has undertaken scenario analysis to assess the impact of such a capital floor. The risks outlined above could have a significant adverse effect on the Bank’s business, operating results, financial condition and/or prospects.

Operational Risk

The Bank faces risks arising from the Bank's underlying business and infrastructure. These are dated and suffer from a lack of integration and investment. There is also an over-reliance on manual intervention in processes, inadequate business continuity and disaster recovery arrangements, poor logical access management and dependencies on inadequate outsourcing arrangements. See the risk factor entitled "*The Bank's operations are highly dependent on the proper functioning of IT and communications systems which are currently in need of urgent and extensive remediation. Any significant delay in or failure of the Bank to remedy the existing IT estate and make improvements in it to meet the requirements of its*

business strategy may adversely affect the future operational and financial performance of the business. The Bank's disaster recovery plan for this IT infrastructure has not been proven, creating a material resilience risk "for further information.

Various elements of operational risk management were previously concluded to be ineffective in 2013, and whilst progress has been achieved in a number of areas, significant work is still required from a people, process and systems perspective to embed an effective and sustainable operational risk framework and to enhance the control culture.

There can be no assurance that further risks and control failings will not be identified, or that the Bank's approach to risk management will prove to be adequate. Such further risk and failings could have a significant adverse effect on the Bank's business, operating results, financial condition and/or prospects.

Conduct Risk

A number of shortcomings have been identified since 2013 in the Bank's compliance with legislation and regulation relating to its offering for mortgages, unsecured loans and credit cards. This requires significant remediation which is in train to redress customers who have suffered detriment from either being offered products not suitable for their needs (PPI) or from poor application of process. Substantial provisions have been made to cover these write-offs both operational as well as redress.

Failure to adequately maintain and protect customer and employee information could have a material adverse effect on the Bank

The Bank and the Group continue to share physical and digital information assets; in particular CFSMS owns the Bank's mainframe which is also shared with CISGIL, therefore creating an increased risk of breaches of data protection and privacy laws and/or industry standards, entailing sanctions and/or fines from regulators (including the Information Commissioners Office in relation to personal data). An adverse finding from a regulator could have an adverse effect on the Bank's reputation and on the Bank's business, operations, financial condition or prospects.

The Bank is dependent on its Directors, senior management team and skilled personnel and the loss of one or more Directors or members of senior management or the loss of or failure to recruit and retain skilled personnel may have an adverse effect on the Bank's business, operating results, financial condition and prospects and its ability to achieve its strategy

The Bank depends on the continued contributions of its Directors, senior management and other key persons with the experience, knowledge and skills in banking necessary for its success. Dennis Holt (former Senior Independent Director) was appointed Chairman effective 27 October 2014 following an internal and external search conducted by Korn Ferry. The Bank now has a search underway to identify a new permanent Senior Independent Director. The process for the nomination of three shareholder nominated directors is underway.

The failure to have succession plans in place for the Chairman, Senior Independent Director and other members of the Board and to recruit and retain non-executive directors in a timely manner to serve on the Board could negatively impact on the effective governance and oversight of the Bank. The executive team have been recruited to implement the Banks' turn around and some or all of them may not wish to remain with the Bank when it begins to operate in a more "business as usual" environment. The loss of one or more members of its executive team without finding suitable replacements or having appropriate succession plans in place, or any adverse perception resulting from the recent change to the Bank's ownership structure, may delay or impact on the ability of the Bank to successfully implement its strategy, lead to a disruption of the business and a loss of specialist knowledge.

The introduction of the regulatory changes governing the senior manager regime which will impact the responsibilities and potential personal liability of Directors and members of senior management may make it more difficult to recruit in the banking industry in general. This could have a greater negative effect on attracting people to work for the Bank in particular as the Bank may be perceived as a more difficult and personally risky regulatory environment in which to work.

The Bank also remains reliant on other personnel employed by members of the Co-operative Group to support separation activities including pensions. In areas where the Bank lacks or does not have a sufficient number of skilled persons, the Bank is reliant on being able to attract and recruit such persons

and to do so within the timescales envisaged by the Bank. Building a team and increased bench strength within the business takes time, and core elements of the Bank's proposals for employees, including a long term incentive scheme, are still in development. The current difficult situation facing the Bank poses further challenges to attracting and retaining appropriately skilled and experienced individuals. Other challenges include the impact of any proposed staff redundancies and cost reductions. Any significant reduction in staff morale may have a consequential impact on service delivery and customer service and, potentially, the Bank's brand, positioning and ability to maintain its retail funding.

The overall "people risk" exposure is currently flagged as a key risk for the Bank in recognition of the level of recruitment required to rebuild the team, business reliance on contractors and the impact of separation. There is no guarantee that the Bank will be able to retain, attract or recruit a sufficient number of appropriately skilled and experienced employees to deliver the required changes and a failure to do so may impact on the Bank's ability to achieve its strategy which, in turn, may negatively impact on its business, operating results, financial condition and prospects.

Union representation subjects the Bank's business to the risk of interruptions through strikes or delays resulting from any restructuring of the Bank or in renegotiating labour contracts

The Bank collectively recognises two trade unions: Britannia Staff Union and Unite. As at 31 December 2014, approximately 68 per cent. of the Bank's employees were union members. While the Bank has not experienced any significant business interruption as a result of labour disputes at any of its businesses since September 2005, and the Bank considers its relations with employees to be sound, the Bank does have a high proportion of staff, including senior individuals, who are members of a trade union. Union representation subjects the Bank's business to increased risk of interruptions through strikes or delays resulting from any restructuring of the Bank or in renegotiating labour contracts.

The Bank's strategy includes a significant cost-cutting exercise, which includes workforce redundancies. In addition, the terms and conditions for the majority of the staff are negotiated through collective bargaining with the unions. The Bank may be unsuccessful in concluding any negotiations with unions or reaching an agreement with the unions, including regarding redundancies. A failure to conclude negotiations and reach agreement, or any protracted negotiations, or any breach of an agreement with the unions may result in interruptions to the business through strikes or delays, a diversion of management time from running the Bank's business and implementing the Bank's strategy, a deterioration in employee relationships, an adverse impact on the Bank's reputation and/or an adverse impact on the Bank's customer relationships. Such interruptions may, in turn, impact on the Bank's business, operating results, financial condition and ability to achieve its strategy.

There can be no assurance that such arrangements will always be in place in the future or that the Bank will be able to continue to negotiate wages and salaries and terms and conditions of employment on terms that support its ability to offer its services at competitive prices.

The contributions that the Bank is required to make to its pension schemes may change over time. The Bank may be obliged to make large one-off payments to its pension schemes, or pension schemes to which it is connected and/or associated, if certain events occur

The Bank is an employer in Pace and is a guarantor of the Britannia Pension Scheme (the "**Britannia Scheme**") (whose sponsoring employer and main participating employer is CFSMS). Pace and the Britannia Scheme are both hybrid/defined pension schemes which provide defined contribution benefits and defined benefits.

Risk arises from these schemes because from time to time there will be insufficient assets to cover the defined benefit liabilities of the scheme (ie there is a deficit in the scheme) and the schemes are therefore creditors of the various employers including the Bank in respect of that deficit. While the actuarial funding deficit will usually set the cash funding demands placed on employers, in some cases the cash demands can be based on the deficit in Pace calculated by reference to the cost of buying out the scheme's liabilities in the insurance market i.e. the buy out basis deficit. The deficits can increase because of changes in market conditions, member longevity, expenses and (in the case of the actuarial funding deficit) changes in the trustees' view of the strength of the participating employers. In such circumstances, the Bank could be obliged to make additional contributions to the schemes, and/or pay in lump sums and/or set aside additional capital in respect of pensions risk. In addition to the ongoing cash demands, liabilities may arise for the Bank as an employer participating in a defined benefit pension

scheme (or as the guarantor of such employers) in certain circumstances set out in legislation, including the winding up of the scheme, on an employer ceasing to participate in the pension scheme or on an employer becoming insolvent. The liability arising (absent an alternative approach to such liability being agreed) will be the value of the employer's share of the buy out deficit at the time.

The most recent triennial valuation of Pace as at 5 April 2013 indicated an actuarial funding deficit of £600 million and estimated the deficit on a buy-out basis of £2,689 million. The actuarial annual update report of Pace as at 5 April 2014 indicated an actuarial funding deficit of £104 million and estimated the deficit on a buy-out basis of £2,265 million. The funding position for the Britannia Scheme at the most recent actuarial annual update report at 5 April 2013 was £61.3 million in deficit. 5 April 2014 is the triennial valuation date and the valuation is not yet finalised.

The employers participating in Pace make aggregate contributions towards the actuarial funding deficit as agreed between the Co-operative Group and the trustees of Pace following the advice of the independent scheme actuary. Thus the Bank does not control how much it may be asked to pay towards the actuarial funding deficit following an actuarial review. Following the most recent valuation of Pace as at 5 April 2013, it has been agreed that the Bank will pay annual contributions towards the actuarial deficit of £5m per annum.

Pace is a "last-man standing scheme", meaning that, while the Bank continues to be an employer in Pace, there is a risk that all employers other than the Bank (including the Co-operative Group) exit Pace or become insolvent without satisfying their liabilities towards the scheme, with the effect that the Bank becomes solely responsible for funding the scheme. The Bank's liability could be up to the level of the entire buy out deficit in Pace.

The Co-operative Group and the Bank have agreed that, subject to certain exceptions, the Co-operative Group cannot force the Bank out of Pace. However, because of the ongoing funding risks and last-man standing risks in relation to Pace as set out above, the Bank may wish to cease to be an employer in Pace. To cease to be an employer in Pace, the Bank must either take its "share" of liabilities into a replacement scheme or pay an lump sum equal to an equivalent share of the buy-out deficit. Paying the lump sum share of the buy out deficit is unlikely to be feasible.

The proportion of Pace liabilities accrued by members while employees of the Bank is believed to represent a minority of total Pace liabilities; however, the employer's share of the liabilities/ deficit may include liabilities that cannot be attributed to any current employer in the scheme. The Bank's revised business plan assumes that, on any separation of Pace, none of these liabilities will be attributed to the Bank. This assumption has been shared with the Co-operative Group which has not yet agreed to it. In the event that material liabilities that cannot be attributed to any current employer are attributed to the Bank if it ceases to be an employer in Pace, this could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

The Co-operative Group and the Bank have agreed that, at either party's request, the parties will enter into good faith discussions to agree a basis on which the Bank can leave Pace, or set up its own segregated section but no arrangements have yet been agreed. There is uncertainty over the amount that the Bank will have to pay in the event that it exits Pace. If the Bank's share of the deficit at the time of exit is greater than expected, significant additional capital may need to be set aside in respect of pensions risk.

If CFSMS becomes insolvent or otherwise ceases to participate in the Britannia Scheme (for example as part of separating the Bank's pension arrangements from the Co-operative Group's), CFSMS could incur a liability equal to most of the buy-out deficit in the Britannia Scheme which would have to be met by the Bank under the terms of the guarantee. It is possible to agree arrangements that would reduce CFSMS's liability on ceasing to participate in the Britannia Scheme. Any such arrangement would require the consent of the trustees of the Britannia Scheme and, in some cases, of the continuing sponsoring employers after CFSMS's exit and the Pensions Regulator. No arrangements have been agreed and there is a risk that none can be agreed.

The Pensions Regulator also has the power to require an employer of a defined benefit scheme or a person connected or associated with it to make a contribution to or provide financial support for that scheme in certain circumstances. There are eight defined benefit pension schemes within the Co-operative Group in addition to Pace and the Britannia Scheme and there is a risk that the Pensions Regulator could impose significant liabilities in respect of any of these Co-operative Group pension

schemes on the Bank. These liabilities could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

The Bank's operations are highly dependent on the proper functioning of IT and communication systems which are currently in need of urgent and extensive remediation. Any significant delay in or failure of the Bank to remedy the existing IT estate and make improvements in it to meet the requirements of its business strategy may adversely affect the future operational and financial performance of the business. The Bank's disaster recovery plan for this IT infrastructure has not been proven, creating a material resilience risk

The Bank relies extensively on IT and communication systems to conduct its business, including the pricing and sale of its products, payment processing, data collection, assessing acceptable levels of risk exposure, setting required levels of provisions and capital, and maintaining customer service and accurate records and security.

A substantial proportion of the Bank systems and technology are on extended support arrangements or end-of-life, there are weaknesses in some internal processes and some of the services which support Bank technology are provided under what are currently inadequate contractual arrangements. See the risk factor entitled "*There are numerous risks associated with the separation of the Bank from its former parent, CBG, and its ultimate former parent, the Co operative Group*" for further information. Due to these issues, extensive IT remediation is urgently required. A remediation programme has commenced but this will not deliver the required reduction in the Bank's residual IT risk position until 2018 at the earliest. Even after any remediation, there remains a risk that the processes and systems may not operate as expected, may not fulfil their intended purposes, or may be damaged or interrupted by disruptive events. Any failure of the IT and communications systems and/or infrastructure on which the Bank relies, including that of the Co operative Group (including CFSMS) or other suppliers, could lead to significant costs and disruptions that could adversely affect the overall operational or financial performance of the business, as well as harm the Bank's reputation and could cause the Bank to breach its obligations as a regulated entity and/or attract increased regulatory scrutiny. Additionally, the Bank's disaster recovery plan for its IT infrastructure is unproven, such that a disruptive event may prevent the Bank from being able to recover its IT infrastructure in a timely manner or at all. This is a material risk. The Bank is undertaking a multi-year IT resilience remediation programme (to which it has committed significant investment) to remediate the critical risks identified. The Bank will continue to be subject to these risks until such time as it has completed its planned remediation activities although incremental improvements will be made as the plan develops. Any failure in systems as a result of not remediating the IT risks, or in the period leading up to such remediation being completed, could adversely affect the Bank's ability to conduct its business and could lead to the PRA and/or the FCA imposing additional requirements (in addition to those discussed below) on the Bank or subjecting the Bank to additional regulatory scrutiny (in addition to the supervision described below). Further, the actual act of working on and changing the legacy IT systems increases the risk of systems failure.

In January 2015, the Bank agreed an outsourcing of its IT enterprise infrastructure services to IBM. The migration to IBM data centres as part of the agreement is expected to provide remediation, simplification and improvements to the IT estate.

The Bank has received written confirmation from the FCA that the Bank not having a proven end-to-end disaster recovery capability constitutes a breach of the threshold conditions forming a part of the high level standards in the FCA Handbook setting out the minimum standards for becoming and remaining an authorised person (the "**FCA Threshold Conditions**"). The FCA is closely supervising the Bank as it works towards restoring compliance with COND 2.4 of the FCA Threshold Conditions as they relate to non-financial resources. The FCA is not currently proposing further immediate supervisory intervention or the immediate exercise of any additional regulatory powers as a result of this assessment. The FCA reserves the right to take action in the future in relation to this breach. The PRA's general policy is not to communicate its assessment of the Bank's position in relation to the PRA Threshold Conditions. The PRA has not communicated to the Bank its assessment of the Bank's position in relation to the PRA Threshold Conditions. The threshold conditions for which the PRA is responsible in relation to the Bank are set out in paragraphs 5A to 5F of Part 1E of Schedule 6 of FSMA. However, both the PRA and FCA are closely monitoring the position of the Bank and the Bank remains in continual dialogue with both regulators. However, there is a risk that the FCA and/or the PRA may take immediate supervisory intervention or exercise any of their regulatory powers in relation to this breach.

The simplification of the IT estate aims to reduce running costs as the IT running costs are currently above the Bank's industry peers. Cost reductions from improvements in IT operating efficiency will also be targeted, although the risk that these reductions do not reduce service below acceptable levels must be managed. The Bank further intends to outsource a significant amount of its IT requirements to accelerate the remediation plan and further manage the costs, although outsourcing brings further risks. See the risk factor entitled "*The Bank is dependent on third-party providers of services, IT, software, data and other assets*" for further information.

The remediation of the IT estate is a significant undertaking and the Bank has a poor track record of successfully implementing large scale changes. Therefore, the remediation involves delivery risk, although this is partially mitigated by the adoption of an improved business change methodology and the selection of experienced delivery partners. Any delays in, or failure by the Bank to deliver the remediation of the IT estate may extend an on-going risk of technology failure, result in significant additional investment costs, subject the Bank to further regulatory scrutiny which may result in the PRA and/or the FCA taking action in relation to any existing and future breaches of threshold conditions and impact the Bank's ability to deliver its business strategy, which may, in turn, adversely affect the future operational and financial performance of the business.

The Bank is dependent on third-party providers of services, IT, software, data and other assets

There is a risk that third-party providers could fail to supply services, IT, software, data or other assets that they have agreed to provide, either adequately or at all. If third-party providers fail to provide or procure the services that they have contracted to provide, or to provide them in a timely manner or to agreed levels, or the arrangements with those providers are terminated for whatever reason, such a failure on termination could have a material adverse effect on the Bank's ability to conduct its business, operating results, financial condition and prospects. Significant failures could lead to a loss of confidence and customers. The Bank may be unable to source an alternative provider for the services, IT, software, data or other assets on a timely basis, on equivalent terms or without significant expense, within the short time required, or at all. The additional costs and expenses incurred in doing so may have a material adverse effect on the Bank's cost base. This could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

There is also a risk that contracts with third-party providers on which the Bank relies may be or may have been poorly negotiated and/or poorly managed, particularly as the Bank has limited experience in negotiating such contracts with third parties. Many of these services are provided by or via the Co-operative Group and CFSMS – this will continue to be the case until the Bank has been able to separate itself completely from the Co-operative Group and CFSMS. See the risk factor entitled "*There are numerous risks associated with the separation of the Bank from its former parent, CBG and its ultimate former parent, the Co-operative Group*" for further information. The risk of poorly negotiated and/or poorly managed contracts will decrease as the Bank reduces its dependencies on the Co-operative Group and CFSMS and continues to build its own internal procurement and supplier management function and to engage more third-party providers.

The Bank has entered into a non-binding letter of intent agreement dated 12 November 2014 with Capita Business Services Limited ("**Capita**") in relation to the proposed outsourcing of its mortgage processing services for all of its residential mortgage portfolios. As part of the proposed transaction, 100 per cent. of the shares in Western Mortgage Services Limited ("**WMS**"), a wholly owned subsidiary of the Bank, would be transferred to Capita. WMS would then acquire the Bank's other mortgage processing and administration operations together and certain existing Bank staff servicing the mortgage portfolios would be transferred to WMS. The Bank's funding programmes that would be impacted by the proposed transaction include: the Moorland Covered Bond Programme, and the Leek, Cambric and Silk Road RMBS Programmes (all as described in note 40 to the consolidated annual accounts of the Bank for the financial year ended 2014, beginning on page 225 of the 2014 Annual Report) and the Warwick Finance One transaction which closed on 6 May 2015. It is proposed that for each impacted programme, the Bank will remain the servicer of record and will sub-delegate servicing to Capita or WMS. Subject to contractual negotiations, due diligence, board approval and relevant regulatory and contractual approvals, it is envisaged that the transaction would complete in 2015. There is a risk that the Bank and Capita may fail to agree to enter into a binding contract to provide such services which would lead to increased costs and a delay in the implementation while the Bank seeks and contracts with an alternative provider.

Any reduction in third-party service or product quality or any failure by a third-party to comply with the Bank's licensing or regulatory requirements, including requirements with respect to the handling of customer data, could cause a material disruption to or adverse financial and/or reputational impact on the Bank's business. Any of these events could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

There are numerous risks associated with the separation of the Bank from its former parent, CBG, and its ultimate former parent, the Co-operative Group

Since mid-2013, when the Liability Management Exercise was initiated, the Bank has been working on operationally separating from its former parent, CBG, its ultimate former parent, the Co-operative Group, and its former sister company, CFSMS. The separation process is complex and time-consuming – the Bank shares premises, systems, personnel and/or services with each of the Co-operative Group and CFSMS and is especially dependent on CFSMS for the provision of shared IT assets and the on-supply of certain third party services under an agreement entered into in 2006 (the "**2006 Agreement**"). While some of these dependencies have since been removed through a transfer of staff and assets from CFSMS to the Bank, a significant degree of dependency remains. The separation process has been continuing for some time but progress has been slower than expected and there are risks associated with execution. The costs of separation have already been significant and further significant costs will likely be incurred.

As part of the separation process, the Bank and members of the Co-operative Group had been renegotiating and updating the terms of existing agreements between them to reflect that they are no longer in the same group (and in some cases putting written agreements in place for the first time). Some of the existing agreements are not on commercial or arm's length terms, including the 2006 Agreement.

The Bank and the Co-operative Group entered into an IT separation costs agreement on 22 January 2015 (the "**IT Separation Costs Agreement**"), which then allowed the Bank to enter into an IT outsourcing agreement with IBM for enterprise computing services (which it entered into on 23 January 2015). Under the IT Separation Costs Agreement, both the Co-operative Group and CFSMS undertake to support activities for the separation of the Bank's IT infrastructure from the wider Co-operative Group's IT infrastructure, to enable the smooth transition to IBM. Further, the Co-operative Group undertakes that any notice to terminate the existing IT services agreement under which IT services are provided to the Bank (the "**IT Services Agreement**") and CFSMS undertakes that any notice to terminate the 2006 Agreement would not take effect prior to 31 December 2017 to give the Bank sufficient time to separate the Bank's IT infrastructure. The IT Separation Costs Agreement also allocated the contributions to be made towards the Co-operative Group's own costs of keeping the wider Co-operative Group's existing IT infrastructure stable and operable during and following the Bank's separation of its IT infrastructure; to this end CBG (as the parent of CFSMS) undertook to contribute a maximum of £95 million towards such Co-operative Group costs, with the Bank to make a contribution of up to £25 million, based on a formula in the event that the total cost of this Co-operative Group project falls between £76 million and £120 million.

As a consequence of the Bank's IT outsourcing agreement with IBM for enterprise computing services, the Bank is not progressing the proposed revised IT Service Agreement and the revised professional services master service agreement (the "**PSMSA**") with the Co-operative Group. A number of service contracts under the PSMSA have now been terminated and services repatriated to the Bank, with the intention that all will be terminated by the end of 2015 except pensions and membership.

As part of IT separation, the Bank and the Co-operative Group have finalised the terms of a data processing agreement, which has three purposes:

(i) to create a legal obligation on both Bank and Co-operative Group to provide to each other, and to each other's subcontractors, the data that is necessary to complete Bank and Co-operative Group IT separation programmes. This includes all data held by each of the parties' group members, which for the Co-operative Group includes CFSMS and CIS General Insurance Limited;

(ii) to establish an appropriate data protection and security framework for the disclosure of data that is shared in order to facilitate the completion of the separation programmes; and

(iii) to provide an appropriate data protection and security framework for all other data sharing that is taking place between the Co-operative Group and the Bank, and their group members, in relation to which no written agreement containing adequate data protection provisions currently exists.

Examples of the risks associated with the separation process are set out below:

- The Bank is currently dependent on members of the Co-operative Group (notably CFSMS) to provide key assets (including shared core IT services and assets, such as the banking platform, prior to the eventual migration to IBM) and to on-supply certain services, data and assets supplied by third-party providers.

  Members of the Co-operative Group have little or no experience in providing outsourcing services to a third party on arm's length terms. For so long as the Bank relies on CFSMS and other members of the Co-operative Group for the provision of assets, services (including third party services) and personnel any failure by CFSMS or another Co-operative Group entity to provide or procure those assets, services or personnel in a timely manner or to agreed levels, could have a material adverse effect on the Bank's business, operating results, financial condition and prospects. For example, the Co-operative Group is not fully in compliance with the Bank's IT security standards. If a security failure should occur, this could materially adversely impact the Bank (e.g. in the form of regulatory fines, reputational damage and/or customer attrition).

- The Bank does not have a documented right to occupy the CIS Tower in Miller Street, Manchester, which is one of its main places of business and which is in the control of the Co-operative Group and which the Bank has historically occupied on an informal basis. Resolution is underway but, if unresolved, this could lead to disputes, additional cost and operational disruption.

- The Bank and the Co-operative Group have entered into a loss sharing deed relating to the surrender of group relief from entities in the Bank's tax group to entities in the Co-operative Group tax group. The deed addresses, amongst other things, the terms on which the Co-operative Group will pay the Bank for tax losses surrendered in relation to the 2012 and 2013 accounting periods. The 2014 Annual Report includes a discounted group relief debtor of £126.8 million. The Bank receives payment from the Co-operative Group when the Co-operative Group realises the benefit of the losses surrendered and at the corporation tax rate at which the benefit is realised. There is a risk that the group relief debtor on the Bank's balance sheet may be reduced if there is a reduction in Co-operative Group's capacity to claim tax losses for the 2012 and 2013 financial periods, there is a decrease in the rate of corporation tax or the Co-operative Group does not generate sufficient taxable profits in the future to realise the benefit of the losses which may, in turn, have a material adverse impact on the Bank's financial condition. For further information, please see paragraph 9.8 (*Loss Sharing Deed*) of the section entitled "*Description of the Bank*".

- The costs of the separation process remain uncertain and may be greater than current forecasts.

- There is a continuing mix of customer, employee and financial data between the Bank and members of the Co-operative Group with limited data partitions or access controls, although the Bank has now finalised the terms of a data processing agreement with the Co-operative Group (described above). Separating this data is likely to be a highly complex process and be impacted by the lack of an information asset register that the Bank will need to compile.

- The separation programme has multiple interdependencies with other programmes (e.g. the IT remediation plan and cost reduction programmes). These interdependencies increase the risk to separation completing in a timely or cost-effective manner.

- There are increased pensions risks. See the risk factor entitled "*The contributions that the Bank is required to make to its pension schemes may change over time. The Bank may be obliged to make large one-off payments to its pension schemes, or pension schemes to which it is connected and/or associated, if certain events occur*" for further information.

- There may be increased potential for conduct issues to arise owing to the extent of change resulting from the separation process.

- CIS General Insurance Limited ("**CISGIL**"), (a Co-operative Group company specialising in the provision of insurance products) and the Bank have been conducting a referral arrangement on an undocumented basis for a number of years, pursuant to which: (i) the Bank markets certain general insurance products provided by CISGIL to its customers; and (ii) CISGIL underwrites PPI for Bank products. The Bank could be exposed to liability for mis-selling products sold under this arrangement. The parties are in the process of negotiating a written referral agreement which intends to, amongst other things, allocate mis-selling liability between the parties by way of a reciprocal indemnity.

Risk that the Bank's insurance cover may be inadequate, that it will be difficult for the Bank to obtain insurance and that those insurance policies which the Bank has in place might become void or voidable

The Bank has a number of insurance policies in place with respect to its business, assets and liabilities. Any insurance that the Bank may obtain may be subject to exclusions, limitations, minimum claim amounts and excess amounts and other terms that mean that the Bank may have uninsured claims and losses. There is therefore a risk that the terms of the Bank's insurance policies will not cover the Bank's liabilities in all situations and that the Bank may therefore have uninsured exposure. There is also a risk that the Bank will not be able to obtain the insurance it needs or expects and in the quantum that it requires, that it might not be able to predict the type of insurance cover it might need and/or that any insurance cover that the Bank does have in place might become void or voidable.

For example, as part of the process of separating from the Co-operative Group, the Bank is in the process of finalising the list of properties and contents. Until such time as the Bank has a complete set of property assets and valuations, there is a risk that the insured values do not fully match the market values of the Bank's assets and therefore do not comply with certain provisions in its property insurance policies. This risks those policies being voidable.

The Bank will continue to rely on the Co-operative Group. The Co-operative Group may also continue to exert substantial influence over the Bank

As at 30 April 2015, the Co-operative Group owned 20.16 per cent. of the issued ordinary share capital of the Bank through CBG.

To the extent it remains a significant shareholder of the Bank (carrying at least 20 per cent. of voting rights), the Co-operative Group will continue to have the power, among other things, to affect or influence the Bank’s legal and capital structure and certain changes to its operations. The interests of the Co-operative Group could conflict with those of the Bank or other shareholders, and this concentration of ownership may also have the effect of delaying, deferring or preventing the Bank’s ability to effect certain types of transactions that require approval by the Co-operative Group. In addition, the separation between the Bank and the Co-operative Group provides a challenge to the Bank’s operating model.

In order to manage these risks, the Bank entered into a Relationship Agreement (as defined in paragraph 9.3 (*Relationship Agreement*) of the section entitled "*Description of the Bank*") with the Co-operative Group which regulates (in part) the relationship between and the degree of control that the Co-operative Group and its subsidiaries may exercise over the Bank as long as the Co-operative Group owns 20 per cent. or more of the Bank. In addition, as referred to in the Relationship Agreement, the Articles of Association of the Bank grant the Co-operative Group the right to appoint one person to the Board of the Bank (see paragraph 9.3 *(Relationship Agreement)* of the section entitled "*Description of the Bank*" for further information).

In the event that the Co-operative Group’s shareholding in the Bank were to fall to below 20 per cent., the Relationship Agreement will terminate. This will have the effect that the Co-operative Group will no longer have the right to appoint a member to the Board of the Bank under the Relationship Agreement or to appoint a member to the Values and Ethics Committee (although the Co-operative Group has the right to nominate a member of the Board under the Variation and Director Appointment Deed (as defined in paragraph 9.4 (*Variation and Director Appointment Deed*) of the section entitled "*Description of the Bank*") provided its shareholding does not fall below 15 per cent.). However, as these provisions are entrenched in the Articles of Association of the Bank, in the event that the Co-operative Group’s shareholding in the Bank increases to over 20 per cent. again, the Co-operative Group’s rights to appoint a member of the Board and a member of the Values and Ethics Committee will be reinstated. Furthermore,

certain provisions of the Relationship Agreement will continue to apply (notwithstanding its termination) in the event that the Co-operative Group's shareholding falls to less than 20 per cent. in the Bank, including the requirements for: (a) the Co-operative Group to use the Bank as its exclusive or principal financial services provider for two years after termination; (b) the Co-operative Group not to operate, establish or acquire a competing business for three years after termination (although the Co-operative Group is permitted to carry on business activities carried on at the date of the when the Liability Management Exercise became unconditional); (c) the Co-operative Group not to solicit for employment any of the directors (or their respective direct reports) or senior managers of the Bank for three years after termination; and (d) the parties to maintain confidentiality.

Under the Shareholder Rights Agreement, the Co-operative Group will in certain circumstances have the right alongside certain other significant shareholders (see paragraph 9.5 (*Shareholder Rights Agreement*) of the section entitled "*Description of the Bank*") to require the Bank to assist in the launch of a secondary offering of ordinary shares, provided the exercising shareholders have committed to sell ordinary shares valued at not less than £100 million.

In addition the Bank continues to be dependent on the Co-operative Group and its subsidiaries for the provision of certain services, including IT. Under the IT Separation Costs Agreement, the IT Services Agreement and the 2006 Agreement may not be terminated for convenience prior to 31 December 2017 to give the Bank sufficient time to separate the Bank's IT infrastructure. However, there can be no guarantee that these arrangements between the Co-operative Group and the Bank will not be interrupted. A significant degree of dependency remains. The separation process has been continuing for some time but progress has been slower than expected and there are risks associated with execution. The costs of separation have already been significant and further significant costs will likely be incurred. For further information, see the risk factor entitled, *"There are numerous risks associated with the separation of the Bank from its former parent, CBG, and its ultimate former parent, the Co-operative Group"* above.

The Bank will continue to rely on the Co-operative brand

The Bank is dependent on the strength of the "Co-operative Bank" brand (which it owns), the wider "Co-operative" brand (as used by the Co-operative Group and other co-operative societies) and its reputation with customers and potential customers of the Bank. Whilst the Bank seeks to manage material risks to the Co-operative Bank brand through careful monitoring, ultimately the Bank is exposed to the risk that the Co-operative Group acts, fails to act or is speculated to act in a way such as to bring the Bank brand into disrepute. This could include litigation, employee misconduct or the misconduct (including criminal activity) of anyone associated with the Co-operative brand (whether through the Co-operative Group, the Bank or otherwise), operational failures, accidents, the outcome of regulatory investigations, press speculation and negative publicity, disclosure of confidential customer information, inadequate products and services, amongst other factors, and could negatively impact the Co-operative brand or the Co-operative Group's reputation. For example, adverse findings about the Co-operative Group arising out of investigations into past actions, or adverse commentary and organisational disruption to the Co-operative Group following the Myners Report on the governance of the Co-operative Group (published 7 May 2014), could adversely affect the Co-operative brand. Should, as a result of matters relating to the Co-operative Group, the Bank's brand, levels of customer satisfaction or the co-operative movement more generally be damaged, this could have a negative effect on the Bank's business, operating results, financial condition and prospects and negatively impact the ability of the Bank to achieve its stated strategy. See the risk factor entitled "*Reputational risk could cause harm to the Bank, its business, operating results, financial condition and prospects and question the Bank's commitment to co-operative values and ethics*" for further information.

The Bank and the Co-operative Group have been negotiating a co-existence agreement in order to allocate trademarks into appropriate ownership, and to govern the use by each party of trademarks such as "Co-op" or "Co-operative" marks, to prevent any likelihood of confusion between the parties' use of such trademarks and to avoid any disputes in the future (the "**Co-Existence Agreement**"). The Bank currently owns the registrations for most of the trademarks that it uses (such as Co-operative Bank), but in the absence of such an agreement there could be greater scope for disagreements on the use of certain shared brands. Furthermore, there are certain trademarks or domain names that the parties are currently discussing the use of which are embedded in the Bank's IT systems and used on existing marketing literature and signage. In the event that the terms of the Co-existence Agreement cannot be agreed there is a risk that the Bank will be required to rapidly make changes to its IT systems, marketing literature and signage to remove these marks (which could have financial implications).

The Bank has entrenched co-operative values and ethics into its Articles of Association. If the Shareholders of the Bank decide to remove those entrenched provisions without the Co-operative Group's consent, the Bank would be obliged, under the Agreed Co-existence Principles, agreed at the time of separation, to cease the conduct of any business under a brand that combines the words "Co-operative" or "Co-op" and "Bank".

There is a risk that the Secretary of State for Business, Innovation and Skills may, under section 76(1) of the Companies Act, direct the Bank to change its registered name if, in his opinion, it gives so misleading an indication of the nature of its activities as to be likely to cause harm to the public. The FCA has the power to prevent the use of the "Co-operative" name, or to take other action regarding the Bank's branding, if the FCA considers this desirable to protect consumers, to promote competition in the interests of consumers or to protect the integrity of the UK financial system (note section 2.55L(2)(c) and (3), section 55N and the FCA's objectives in section 1C, 1D and 1E of FSMA).

The Bank's accounting policies and methods are critical to how it reports its financial condition and results of operations. They require the Bank to make estimates about matters that are uncertain

The preparation of financial statements in accordance with the international financial reporting standards issued by the IASB as adopted by the European Commission for use in the EU ("**IFRS**") requires the use of estimates. It also requires management to exercise significant judgement in applying relevant accounting policies so that they comply with IFRS.

In the Bank's financial statements, the basis of preparation and accounting policies disclosures have identified certain accounting policies in respect of which significant judgement is required in determining appropriate assumptions and estimates when valuing assets, liabilities, commitments, provisions and contingencies. There is a risk that if the judgement exercised or the estimates or assumptions used subsequently turn out to be incorrect then this could result in significant loss to the Bank, beyond that anticipated or provided for, which could have an adverse impact on the Bank's operations, financial results and condition.

These critical judgements and estimates relate to, *inter alia*, the assumptions used in the determination of loan impairment provisions, conduct risk and legal provisions, the treatment of assets held by CFSMS, intangible and tangible assets impairments, deferred tax, pension schemes and the Liability Management Exercise.

A variety of factors could affect the ultimate value that is obtained either when earning income, recognising an expense, recovering an asset or reducing a liability. The Bank has established policies and control procedures that are intended to ensure that these judgements (and the associated assumptions and estimates) are well controlled and applied consistently. In addition, the policies and procedures are intended to ensure that the process for changing methodologies occurs in an appropriate manner. The Bank cannot guarantee that it will not be required to make (potentially material) changes in accounting estimates or restate prior period financial statements in the future. Ernst & Young LLP were appointed as auditors in 2014 and this change in auditors could affect the interpretation of accounting policies and practices.

The processes for consolidating the Bank's financial results are manual in nature and involve significant spreadsheet overlays. The processes are reliant on checks and reconciliations to ensure accuracy of the results reported, and are resource intensive

The Bank's financial reporting process is complex, reflecting reliance on legacy systems which have not been integrated following the merger of the Bank and Britannia. The Bank relies on manual processes to consolidate the Bank's financial results, and there is a significant use of spreadsheets, as opposed to automated consolidation processes. The manual nature of the processes increases the risk of accounting errors.

The Bank's statutory results and management accounts, drawn from five different ledgers, are consolidated in spreadsheets, rather than by use of automated consolidation processes, with adjustments also being made. The manual nature of the processes and reconciliations increases the risk of accounting errors, although the Bank has implemented controls and checks to help ensure the accuracy of the financial results.

There is an on-going project to improve the monthly results process, and whilst the Bank continues to make progress, these risks will not be fully remediated for some time, requiring significant investment in technology and business process change, in 2015 and beyond. Further technology improvements are envisaged in both 2015 and 2016. As part of this activity, processes and teams have been, and will continue to be, relocated and there is a risk of lost knowledge and expertise from the current spreadsheet based processes. Additional recent regulatory requirements, including FINREP and COREP have created further strain on these processes and will continue to do so until they have been fully automated. These improvements and automations may take longer or prove to be more expensive than currently anticipated.

These risks could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

Provisions for liabilities in the Bank's accounts may not be adequate

Provisions are recognised for legal or constructive obligations arising from past events, if it is probable (i.e. more likely than not) that there will be outflows of resources and the amounts can be reliably estimated. Contingent liabilities are possible obligations whose existence will be confirmed only by uncertain future events or present obligations where the transfer of economic resources is uncertain and cannot reasonably be measured. Contingent liabilities are not recognised on the balance sheet, but are disclosed unless the outflow of resources is remote. These liabilities may be underestimated or there may be liabilities of which the Bank is currently unaware.

Where provisions have already been taken in published financial statements or results announcements, these have been recognised, in accordance with IAS 37 "*Provisions, Contingent Liabilities and Contingent Assets*", as the best estimate of the expenditure required to settle the obligation as at the reporting date. Such estimates are inherently uncertain and it is possible that the eventual outcomes may differ materially from current estimates, resulting in future increases or decreases to the required provisions (as has, for example, been the case in relation to the provisions that the Bank has made in relation to PPI redress payments), or actual losses that exceed or fall short of the provisions taken. Examples of contingent liabilities in relation to which this risk might apply include provisions in respect of conduct and legal risk, pensions and certain tax and indemnities relating to the Bank's separation from the Co-operative Group.

Changes in the Bank's accounting policies or in accounting standards could materially affect how it reports its financial condition and operating results

From time to time, the International Accounting Standards Board (the "**IASB**") and/or the EU change the IFRS that govern the preparation of the Bank's financial statements. These changes can be difficult to predict and could materially impact how the Bank records and reports its financial condition and results of operations. In some cases, the Bank could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements.

For example, changes to International Financial Reporting Standard 9 (Financial Instruments: Recognition and Measurement) ("**IFRS9**")**,** which are due to become effective in relation to accounting periods beginning on or after 1 January 2018, are likely to have a material impact on Bank in relation to hedge accounting and the measurement and impairment of financial instruments.

The IASB may make other changes to financial accounting and reporting standards that govern the preparation of the Bank's financial statements, which the Bank may adopt, or which the Bank may adopt prior to the date on which such changes become mandatory if determined to be appropriate by the Bank, or which the Bank may be required to adopt. Any such change in the Bank's accounting policies or accounting standards could materially affect its reported financial condition and results of operations.

The Bank's business and financial performance has been and may continue to be affected by general economic conditions in the UK, and adverse developments in the UK or global financial markets could cause the Bank's earnings and profitability to decline

The Bank is directly and indirectly subject to inherent risks arising from general economic conditions in the UK and other economies and the state of the global financial markets both generally and as they specifically affect financial institutions. Since mid-2008, the global economy and the global financial system, have experienced a period of significant turbulence and uncertainty. The severe dislocation of the

financial markets around the world that began in August 2007 and significantly worsened in mid-2008 triggered widespread problems at many commercial banks, investment banks and other financial and related institutions in the UK and around the world. The dislocation severely impacted general levels of liquidity, the availability of credit and the terms on which credit is available. This crisis in the financial markets led the Government and other governments to inject liquidity into the financial system and take other forms of action relating to financial institutions, including bank recapitalisations and the provision of government guarantees for certain types of funding, aimed at both supporting the sector and providing confidence to the market. There can be no guarantee of such support in the future, and such support is likely to be on more punitive terms for financial institutions than in the past.

These market dislocations were also accompanied by recessionary conditions and trends in the UK and many economies around the world. The widespread deterioration in these economies affected, among other things; consumer confidence, levels of unemployment, the housing market, the commercial real estate sector; bond markets, equity markets, counterparty risk, inflation, the availability and cost of credit, transaction volumes in wholesale and retail markets, the liquidity of the global financial markets and market interest rates, which in turn had, and continues to have, in a number of respects, a material adverse effect on the Bank's business, operating results, financial condition and prospects.

A sovereign debt crisis in Europe led to an increase in the cost of funding. The initial impact of this increase was felt in the wholesale markets, and there was a consequential increase in the cost of retail funding, with greater competition in the market for savings. The potential exit of Greece from the EU may also lead to uncertainty within European financial markets.

A number of policy interventions, including most recently the Bank of England's "Funding for Lending Scheme", have helped to ease these funding pressures. However, if there were to be further escalations in the European sovereign debt crisis, the cost of funding could increase again.

There remain continued challenges and uncertainty for the UK economy, including the combined economic prospects of the Eurozone, which presents a risk of a slowdown in economic activity in the UK's principal export markets, the impact of any future government austerity measures, and the continued squeeze on household incomes.

These pressures on households may, if combined with an increase in interest rates, lead to an increase in arrears in the Bank's residential lending portfolios, including Optimum (as described in paragraph 3(C.3)(a) of the section entitled "*Description of the Bank*") and an associated increase in retail impairment provisions.

Whilst there have recently been improvements in UK GDP and the commercial and residential property markets, macroeconomic risk remains. Should a reversal of the improvements occur or the improvements of other factors lead to increased interest rates, these could have a potential impact on impairments; for further information see the risk factor entitled "*Worsening economic and market conditions could result in increased commercial property loan losses beyond what the Bank has already provided for, which would adversely impact the Bank's financial and operational performance*" for further information.

The continued effect of margin compression and exposure to both retail and commercial loan impairment charges, resulting from the impact of general economic conditions, means that the results of the Bank's operations and financial position may continue to be adversely impacted by such factors, and there remains the possibility of further downward pressure on its operating results and financial condition, prospects and growth depending on a number of external influences, such as the consequences of a more austere economic environment.

A referendum on UK membership of the European Union (expected before the end of 2017) may affect the Bank's risk profile through introducing potentially significant new uncertainties and instability in financial markets ahead of the date of the referendum and, depending on the outcome, after the event. These uncertainties could have a material adverse effect on the Bank's business, financial condition, results of operations and prospects.

The Bank's earnings and net interest margins have been adversely affected by a number of factors, and may continue to be adversely affected for so long as one or more of these factors persist. In addition, regulatory capital shortfall and other recent events impacting the Bank may have an adverse effect on the Bank's net interest margin

The Bank's net interest margin and, consequentially, earnings are affected by the pricing on the lending products it offers to its customers and the cost of funding. The Bank's net interest margin has been squeezed by a number of factors which have negatively impacted on the pricing of its lending products and the cost of its funds, such as the low level of the Bank of England base rate since March 2009 and competition in retail funding and lending markets. These factors may continue to adversely affect the Bank's net interest margin for so long as one or more of these factors persist. In addition, the regulatory capital shortfall and other recent events impacting the Bank may have an adverse effect on the Bank's net interest margin.

Competition for the highest quality mortgages is intense and is likely to continue, putting downward pressure on returns available for the lowest risk-weighted mortgage assets.

Worsening economic and market conditions and/or increasing interest rates and/or a fall in house prices could result in increased residential mortgage and unsecured loan losses which would adversely impact the Bank's financial and operational performance

The personal borrowing sector in the UK remains heavily indebted and vulnerable to increases in unemployment, rising interest rates and/or falling house prices.

Increased unemployment could lead to higher levels of arrears, in both the Bank's retail residential mortgage loan and unsecured consumer loan portfolios which, in turn, would lead to an increase in the Bank's impairment charges in respect of these portfolios. Increased unemployment could also result in less demand for the Bank's products.

Rising interest rates would put pressure on existing and new borrowers whose loans are linked to the base rate or LIBOR or the Bank's variable rates and who may have become accustomed to the current low interest rate environment. A significant portion of the Bank's outstanding residential mortgage loan products are potentially subject to changes in interest rates. In particular, Optimum, being a portfolio of predominantly interest-only intermediary and mortgage book assets (as at 31 December 2014, £6,822.9 million) may be particularly sensitive to changes in interest rates as they impact affordability, particularly in stressed economic scenario forecasting. In an increasing interest rate environment, borrowers seeking to avoid increased monthly payments caused by interest rate increases by refinancing their mortgage loans may no longer be able to find available replacement loans at comparably low interest rates and this could lead to an increase in arrears in the Bank's secured lending portfolios, as well as an increase in the Bank's secured loan impairment charges. The majority of the unsecured loan portfolio is on fixed customer rates.

If UK house prices were to fall generally or in particular regions to which the Bank has significant exposure, this would likely to result in an increase in the Bank's secured loan impairment charges as the value of the security underlying its mortgage loans was eroded. In addition, a key assumption in the judgment of estimated future credit losses is the Bank's estimate of future house price index movements. Optimum, which had an average loan-to-value of 73 per cent. as at 31 December 2014, is particularly exposed to movements in house prices.

In addition, increasing interest rates could trigger unforeseen movements in the Bank's existing mortgage portfolio; in particular in relation to accelerated run off of demand savings balances or standard variable rate mortgage balances, as customers perceive that there is greater incentive to review their finances. This could adversely affect the Bank's operational and financial performance.

Worsening economic and market conditions could result in increased commercial property loan losses beyond what the Bank has already provided for, which would adversely impact the Bank's financial and operational performance

The Bank's portfolio of loans secured on commercial property amounted to £3.9 billion at 31 December 2014. The underlying credit quality of these loans has been negatively impacted by continued poor

economic conditions. These commercial loans have already been significantly impaired prior to being placed into run-off.

However, the commercial property market is still adversely affected by:

i. a fall of commercial property valuations;

ii. lower availability of debt and equity finance to support restructurings;

iii. uncertain capital treatment regime of commercial real estate lending;

iv. several high-profile tenant failures in recent years; and

v. market trends for shorter lease life and of tenants exercising breaks.

These factors reduce cash flow certainty and exacerbate collateral values volatility and difficulties in refinancing. It is possible that collateral values may decline further in the next few years, particularly in secondary office and retail properties, resulting in further impairments of the Bank's remaining commercial loan property portfolio, which could have a material adverse effect on the Bank's business, operating results, financial condition and prospects.

The Bank is exposed to a number of tax risks including risk of changes in tax legislation and its interpretation and a change in the rate of corporate and other taxes

The Bank's activities are conducted principally in the UK and it is, therefore, subject to a range of UK taxes at various rates. Changes to tax law, tax rates and penalties for failure to comply could have a material adverse effect on the Bank's business, its financial condition and prospects and/or results of the Bank's operations.

Risks relating to the Notes

The Notes are capital instruments of the Issuer and will absorb losses ahead of unsubordinated liabilities of the Issuer. Losses in respect of the Notes are not covered by the Financial Services Compensation Scheme

The Notes are subordinated capital securities of the Bank and are not protected by the FSCS. The Notes will, upon issue, form part of the regulatory capital of the Bank. Banks are required to hold regulatory capital to absorb losses (before depositors and other senior creditors suffer losses), including during periods of financial stress. As a provider of capital to the Bank, an investor in the Notes should be prepared to suffer losses on its investment if, in particular, the Bank and/or the financial sector generally approaches or enters into a period of financial stress. Such losses could be manifested in a number of ways, including (without limitation) that the market price of the Notes may fall significantly, the United Kingdom authorities could take action under the Banking Act (or similar future legislation), or the Bank could enter into an insolvent winding-up, with the result that investors in the Notes could lose all or substantially all of their initial investment in the Notes. Since the Notes are not protected by the FSCS, the FSCS will not pay any compensation to an investor under these, or any other, circumstances. Accordingly, an investor in the Notes may lose some, or the entire amount of, its investment in the Notes.

The Bank is subject to the UK Banking Act. The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK banks, investment firms and certain of their affiliates in the event a bank or investment firm in the same group is considered to be failing or likely to fail. Furthermore, such actions can be taken directly against any relevant entity or against certain of its UK group companies. The exercise of any of these actions in relation to the Bank could materially adversely affect the value of the Notes, or could result in the principal amount of the Notes being written down or written off entirely

Under the Banking Act, substantial powers are granted to the Bank of England (or, in certain circumstances, HM Treasury), in consultation with the PRA, the FCA and HM Treasury, as appropriate (together, the "**Authorities**") as part of a special resolution regime (the "**SRR**"). These powers enable the Authorities to deal with a UK bank, building society or investment firm (each referred to herein as "UK bank") and certain of their affiliates (each a "**relevant entity**") in circumstances in which the relevant Authority considers its failure has become likely and if certain other conditions are satisfied (depending

on the relevant power), for example to protect and enhance the stability of the financial system of the UK. The SRR consists of five stabilisation options and two insolvency and administration procedures applicable to UK banks which may be commenced by the Authorities. The stabilisation options available to the relevant Authority under the SRR provide for:

(i) private sector transfer of all or part of the business of the relevant entity;

(ii) transfer of all or part of the business of the relevant entity to a "bridge bank" established by the Bank of England;

(iii) transfer of all or part of the business of the relevant entity to an asset management vehicle owned and controlled by the Bank of England;

(iv) writing down certain claims of unsecured creditors of the relevant entity (such as the Notes) and/or converting certain unsecured debt claims (such as the Notes) to equity, which equity could also be subject to any future write-down (the "**bail-in option**"); and

(v) temporary public ownership (nationalisation) of all or part of the relevant entity.

In addition, the Banking Act provides the Authorities with the power to permanently write-down or convert capital instruments, such as the Notes, into equity at the point of non-viability and before any other resolution action is taken. Any shares issued to holders of the Notes upon any such conversion into equity may also be subject to any application of the bail-in option and other resolution powers.

The point of non-viability under the Banking Act is the point at which the relevant Authority determines that the relevant entity meets certain conditions (but no resolution action has yet been taken) or that the relevant entity or, in certain circumstances, group will no longer be viable unless the relevant capital instruments (such as the Notes) are written-down or converted. See further "*Mandatory write-down and conversion of capital instruments may affect the Notes, which may result in Noteholders losing some or all of their investment in the Notes*" below.

Each of these stabilisation options is achieved through the exercise of one or more "stabilisation powers", which include: (i) the power to make share transfer orders pursuant to which all or some of the securities issued by a relevant entity may be transferred to a commercial purchaser, a bridge bank or, in the case of certain relevant entities, the UK government; (ii) the resolution instrument power which may make provision for bail-in; (iii) the power to transfer all or some of the property, rights and liabilities of relevant entity to a commercial purchaser or Bank of England entity; and (iv) the third country instrument powers that recognise the effect of similar special resolution action taken under the law of a country outside the EEA (a "**Third Country**"). A share transfer order can extend to a wide range of securities, including shares and bonds issued by a relevant entity and warrants for such shares and bonds and could, therefore, apply to the Notes. Exercise of these powers could involve taking various actions in relation to any securities issued by the Issuer (including the Notes) without the consent of the holders, including (among other things) (i) transferring the Notes notwithstanding any restrictions on transfer and free from any trust, liability or encumbrance; (ii) delisting the Notes; (iii) writing down the principal amount of the Notes and/or converting the Notes into another form or class (which may include, for example, conversion of Notes into equity securities); and/or (iv) modifying or disapplying certain terms of the Notes, including disregarding any termination or acceleration rights or events of default under the terms of the Notes which would be triggered by the exercise of the powers and certain related events. In addition, the Banking Act grants powers to modify contractual arrangements in certain circumstances, powers to suspend enforcement or termination rights that might be invoked as a result of the exercise of the resolution powers and powers for the relevant Authority to disapply or modify laws (with possible retrospective effect) to enable the powers under the Banking Act to be used effectively.

The exercise of any resolution power or any suggestion of any such exercise could materially adversely affect the value of any Notes and could lead to Noteholders losing some or all of the value of their investment in the Notes. In such circumstances, Noteholders may have a claim for compensation under one of the compensation schemes existing under, or contemplated by, the Banking Act, but there can be no assurance that Noteholders would thereby recover compensation promptly or equal to any loss actually incurred.

The SRR is designed to be triggered prior to insolvency of the relevant Issuer and Noteholders may not be able to anticipate the exercise of any resolution power by the relevant Authority

The stabilisation options are intended to be used prior to the point at which any insolvency proceedings with respect to the relevant entity could have been initiated. The purpose of the stabilisation options is to address the situation where all or part of a business of a relevant entity has encountered, or is likely to encounter, financial difficulties, giving rise to wider public interest concerns. Accordingly, the stabilisation options may be exercised if (a) the relevant Authority is satisfied that a UK bank (such as the Bank) is failing, or is likely to fail, (b) following consultation with the other Authorities, the relevant Authority determines that it is not reasonably likely that (ignoring the stabilisation powers) action will be taken by or in respect of a UK bank that will result in condition (a) above ceasing to be met, (c) the relevant Authority considers the exercise of the stabilisation powers to be necessary, having regard to certain public interest considerations (such as the stability of the UK financial system, public confidence in the UK banking system and the protection of depositors, being some of the special resolution objectives) and (d) the relevant Authority considers that the special resolution objectives would not be met to the same extent by the winding-up of the UK bank.

Pursuant to section 7 of the Banking Act, a UK bank will be considered as failing or likely to fail when, but for financial assistance (if any) provided by HM Treasury or the Bank of England (disregarding ordinary market assistance offered by the Bank of England on its usual terms): it is, or is likely in the near future to be, failing, or likely to fail, to satisfy the PRA Threshold Conditions where such failure would justify the variation or cancellation of the relevant UK bank's permission under FSMA to carry on one or more regulated activities; the value of its assets is, or is likely in the near future to be, less than its liabilities; it is, or is likely in the near future to be, unable to pay its debts or other liabilities as they fall due; or it requires extraordinary public financial support (and such support does not fall within certain limited circumstances).

In the event that the Authorities seek to exercise their powers in relation to a UK banking group company, the relevant Authority has to be satisfied that (A) the conditions set out in (a) to (d) above are met in respect of a UK bank in the same banking group (or, in respect of an EEA or Third Country credit institution or investment firm in the same banking group, the relevant EEA or Third Country resolution authority is satisfied that the conditions for resolution applicable in its jurisdiction are met) and (B) certain criteria are met, such as the exercise of the powers in relation to such UK banking group company being necessary having regard to public interest considerations. The use of different stabilisation powers is also subject to further "specific conditions" that vary according to the relevant stabilisation power being used.

Although the Banking Act provides for the conditions described above to the exercise of any resolution powers, it is uncertain how the relevant Authority would assess such conditions in different pre-insolvency scenarios affecting the relevant Issuer and/or other members of its group and in deciding whether to exercise a resolution power. The relevant Authority is also not required to provide any advanced notice to Noteholders of its decision to exercise any resolution power. Therefore, Noteholders may not be able to anticipate a potential exercise of any such powers nor the potential effect of any exercise of such powers on the relevant Issuer, its group and the Notes.

The bail-in option may be exercised in respect of all liabilities not excluded or protected, including the Notes, which may result in Noteholders losing some or all of their investment in the Notes

The bail-in option has been introduced as an additional tool available to the relevant Authority, to enable it to recapitalise a failed institution by allocating losses to its shareholders and unsecured creditors (which includes Noteholders) in a manner that (i) ought to respect the hierarchy of claims in an ordinary insolvency and (ii) is consistent with shareholders and creditors not receiving a less favourable treatment than they would have received in ordinary insolvency proceedings of the relevant entity (known as the "no creditor worse off" safeguard). Certain liabilities are excluded from the scope of the bail-in tool, such as insured deposits and liabilities to the extent they are secured. The Banking Act also grants the powers for the relevant Authority to exclude any liability or class of liabilities on certain prescribed grounds (including financial stability grounds) and subject to specified conditions.

The bail-in option includes the power to cancel a liability or modify the terms of contracts for the purposes of reducing or deferring the liabilities of the relevant entity under resolution and the power to convert a liability from one form or class to another. The exercise of such powers may result in the

cancellation of all, or a portion, of the principal amount of, interest on, or any other amounts payable on, the Notes and/or the conversion of all or a portion of the principal amount of, interest on, or any other amounts payable on, the Notes into shares or other securities or other obligations of the Bank or another person, including by means of a variation to the terms of the Notes, in each case, to give effect to the exercise by the relevant Authority of such power.

Where the relevant statutory conditions for intervention under the SRR and the use of the bail-in tool have been met, the relevant Authority would be expected to exercise these powers without the consent of the Noteholders.

In accordance with the principles established for the exercise of the bail-in option, the relevant Authority will be required to have regard to the hierarchy of claims in an ordinary insolvency. Therefore, the Bank expects that the relevant Authority would, in any exercise of the bail-in powers, write-down or convert any eligible liabilities of the Bank that rank junior to the Notes before exercising its bail-in powers in respect of the Notes.

The exercise of any resolution power, including the bail-in powers in relation to the Bank or any suggestion of any such exercise could materially adversely affect the rights of the Noteholders, the price or value of their investment in the Notes and/or the ability of the Bank to satisfy its obligations under the Notes and could lead to Noteholders losing some or all of the value of their investment in such Notes. In addition, even in circumstances where a claim for compensation is established under the 'no creditor worse off' safeguard in accordance with a valuation performed after the resolution action has been taken, it is unlikely that such compensation would be equivalent to the full losses incurred by the Noteholders in the resolution and there can be no assurance that Noteholders would recover such compensation promptly.

As insured deposits are excluded from the scope of the bail-in tool and other preferred deposits (and insured deposits) rank ahead of any Notes issued by the Bank, such Notes would be more likely to be bailed-in than certain other unsubordinated liabilities of the Bank (such as other preferred deposits)

As part of the reforms required by the BRRD, amendments have been made to relevant legislation in the UK (including the Insolvency Act 1986) to establish a statutory preference in the insolvency hierarchy (i) firstly, for deposits that are insured under the FSCS ("insured deposits") to rank with existing preferred claims as "ordinary" preferred claims and (ii) secondly, for certain other deposits of individuals and micro, small and medium sized enterprises held in EEA or non-EEA branches of an EEA bank ("other preferred deposits"), to rank as "secondary" preferred claims only after the "ordinary" preferred claims. In addition, the DGSD, which is to be implemented into national law by July 2015, will increase the nature and quantum of insured deposits to include a wide range of deposits, including corporate deposits (unless the depositor is a public authority or financial institution) and some temporary high value deposits. The effect of these changes is generally to increase the size of the class of preferred creditors. All such preferred deposits will rank in the insolvency hierarchy ahead of all other unsecured senior creditors of the Bank, including the Noteholders. Furthermore, insured deposits are excluded from the scope of the bail-in tool. As a result, the Notes issued by the Bank would be more likely to be bailed-in than certain other unsubordinated liabilities of the Bank such as other preferred deposits.

Mandatory write-down and conversion of capital instruments may affect the Notes, which may result in Noteholders losing some or all of their investment in the Notes

The recent amendments to the Banking Act to implement the BRRD have introduced, in addition to the bail-in resolution tool, the requirement for the relevant Authority to permanently write-down, or convert into equity, Tier 1 capital instruments and Tier 2 capital instruments (such as the Notes) at the point of non-viability of the relevant entity and before any stabilisation power is exercised (except in the case of an exercise of the bail-in power to include other liabilities, when such instruments would be written down or converted into equity pursuant to the exercise of the bail-in power, as described above, rather than the mandatory write-down and conversion power).

For the purposes of the application of such mandatory write-down and conversion power, the point of non-viability is the point at which the relevant Authority determines that the relevant entity meets the conditions for resolution (but no resolution action has yet been taken) or that the relevant entity will no longer be viable unless the relevant capital instruments are written-down or converted or the relevant

entity requires extraordinary public support without which, the relevant Authority determines that, the relevant entity would no longer be viable.

Noteholders may be subject to write-down or conversion into equity on application of such powers (without requiring such Noteholders' consent), which may result in such Noteholders losing some or all of their investment. The "no creditor worse off" safeguard would not apply in relation to an application of such powers. The exercise of such mandatory write-down and conversion power under the Banking Act or any suggestion of such exercise could, therefore, materially adversely affect the rights of Noteholders, the price or value of their investment in the Notes and/or the ability of the Bank to satisfy its obligations under the Notes.

Minimum requirement for own funds and eligible liabilities

In order to ensure the effectiveness of bail-in and other resolution tools, the BRRD requires that all institutions must meet an individual MREL requirement, calculated as a percentage of total liabilities and own funds and set by the relevant resolution authorities. Items eligible for inclusion in MREL will include an institution's own funds along with "eligible liabilities". The UK has opted to defer the implementation of the MREL regime until 1 January 2016.

The European Banking Authority (the "**EBA**") and the European Commission are required to develop the criteria for determining the MREL, the calculation methodologies and related measures. Although the EBA has consulted on certain proposals, which are in draft form and subject to change, the precise impact of the MREL requirements on individual firms will remain a matter of some uncertainty until the final measures are adopted. It is also unclear whether the proposals published in November 2014 by the Financial Stability Board ("**FSB**") for a new international standard on total loss absorbing capacity ("**TLAC**") for globally systemically important banks ("**G-SIBs**") (albeit the Bank not being a G-SIB based on the latest FSB list published in November 2014) will affect the way in which the authorities implement the MREL regime.

While these measures remain in development, it is not possible to determine the ultimate scope and nature of any resulting obligations for the Bank or its group, nor the impact that they will have on the Bank or its group once implemented. If FSB's and EBA's proposals are implemented in their current form however, it is possible that the Bank and/or other members of its group may have to issue MREL eligible liabilities in order to meet the new requirements within the required timeframes and/or that these proposals would impose operational restrictions on the Bank's group, increase the Bank's group's expenses and/or otherwise have a material adverse effect on the business, financial condition, results of operations and/or prospects of the Bank and/or its group and, in turn, adversely affect the value of the Notes. Furthermore, the Bank has euro 500 million of senior unsecured debt issued under its euro medium term note programme that will mature in October 2015. While the Bank does not need to raise additional capital for the working capital needs of the Bank (due it its current excess liquidity position), it remains a key component of the Bank's revised business plan to raise additional non-CET 1 capital for regulatory capital purposes, including for the purposes of having liabilities available for the purposes of any exercise of the bail-in tool as well as to potentially count towards the total available eligible liabilities position of the Bank that may be required to satisfy MREL requirements which are due to be implemented into the UK from 2016. Depending on the scope of the MREL rules that are implemented in the UK, the maturity of the Bank’s euro 500 million debt issue may reduce the Bank’s total eligible liabilities requirement for MREL although the issuance of other debt instruments such as the issue of the Notes and other planned tier 2 issuance would be expected to contribute to the Bank’s overall eligible requirements position under MREL. There is a risk that any failure to issue the Notes and other planned tier 2 capital would reduce the total available eligible liabilities position of the Bank that may be required to satisfy MREL requirements which are due to be implemented into the UK from 2016. The ultimate scope and nature of how the MREL may be implemented, including any transitional arrangements, in the UK is still to be finalised; however, it is possible, once it is implemented, that any failure to comply with the MREL regime as implemented may lead to the PRA, at its discretion, electing to exercise one or more of its various powers over the Bank.

The Issuer's obligations under the Notes are subordinated and, on a winding-up of the Issuer, a holder may lose some or all of its investment in the Notes

The Issuer's obligations under the Notes will constitute unsecured and subordinated obligations of the Issuer.

In a winding-up of the Issuer, all obligations of the Issuer which are unsubordinated (including its obligations to depositors in respect of their deposits), and any other obligations which rank senior to the Notes, must be satisfied in full before any assets of the Issuer are applied to satisfying the claims of the holders in respect of the Notes. Further, any claims in the winding up which rank *pari passu* with the claims of the Noteholders in respect of the Notes will be met on a pro rata basis together with the claims of the Noteholders. Accordingly, in such circumstances, if the assets of the Issuer are insufficient to satisfy in full the claims ranking ahead of the claims in respect of the Notes, the Noteholders will lose their entire investment in the Notes and, if the assets of the Issuer are sufficient to satisfy in full those senior-ranking claims but not the claims of the Notes and all other claims ranking *pari passu* with the Notes, the holders will lose some (which may be substantially all) of their investment in the Notes.

There is no restriction on the amount or type of further securities or indebtedness that the Issuer may issue, incur or guarantee

There is no restriction on the amount or type of further securities or indebtedness that the Issuer may issue, incur or guarantee, as the case may be, that rank senior to, or *pari passu* with, the Notes. The issue or guaranteeing of any such further securities or indebtedness may reduce (including to nil) the amount recoverable by Noteholders under the Notes on a winding-up or dissolution of the Issuer. In addition, the Notes do not contain any restriction on the Issuer issuing securities which may have preferential rights to the Notes.

There is no active trading market for the Notes

The Notes are new securities which may not be widely distributed and for which there is currently no active trading market. If the Notes are traded after their initial issuance, they may trade at a discount to their initial offering price, depending upon prevailing interest rates, the market for similar securities, general economic conditions and the financial condition of the Issuer. Although application has been made for the Notes to be admitted to listing on the Official List of the FCA and to trading on the regulated market of the London Stock Exchange, there is no assurance that such application will be accepted or that an active trading market will develop. Further, if the Notes are traded, the trading prices may be volatile, and such volatility may increase if the Bank's capital ratios deteriorate or the Bank otherwise suffers periods of financial stress, in particular if such deterioration results, or is expected to result, in any resolution or other action being taken in respect of the Bank under the Banking Act, as the same may be amended. Recent developments, especially in the European sovereign debt markets (including uncertainties surrounding the finances of the Hellenic Republic) and the possible evolution of monetary policies, together with the reduced risk and inventory capacity of market-makers, have also at times reduced the depth of and increased the volatility of the secondary markets in bank capital instruments such as the Notes. Accordingly, there is no assurance as to the development or liquidity of any trading market for the Notes, and if investors wish to sell their Notes there can be no assurance that they will be able to do so or that, if they are able to sell their Notes, they will obtain a price equivalent to that at which they purchased the Notes.

The Notes may be redeemed prior to maturity at the sole option of the Issuer, and investors may be unable to reinvest the proceeds of redemption at a similar rate of return

The Issuer may, in its sole discretion and subject as provided in Condition 6 (*Redemption and Purchase*), elect to redeem the Notes at their principal amount, together with any accrued interest, on 1 July 2020 or, upon the occurrence of a Tax Event or a Regulatory Event, at any time. In such circumstances an investor may not be able to reinvest the redemption proceeds in a comparable security at an effective interest rate as high as that of the Notes.

Holders of the Notes will have limited rights of enforcement

The Trustee, on behalf of the Noteholders, is entitled to enforce the payment obligations of the Issuer in respect of the Notes only by instituting proceedings for, and/or proving in, the winding-up of the Issuer, and the principal amount of the Notes shall only be capable of being accelerated in the event of a winding-up (save that the Notes will not be accelerated where such winding-up is for the purposes of a reconstruction or amalgamation on terms previously approved in writing by the Trustee). There is no right of acceleration in the case of non-payment of principal or interest on the Notes except in a winding-up of the Issuer, and neither the holders nor the Trustee shall be entitled to institute proceedings for the

winding-up of the Issuer in the event that the Issuer fails to perform any of its obligations (other than an obligation to pay interest or principal) under or in respect of the Notes.

Accordingly, the sole remedy against the Issuer available for recovery of amounts owing in respect of any non-payment of any amount that has become due and payable under the Notes is for the Trustee to institute proceedings for the winding-up of the Issuer, and the Trustee shall not be under any obligation to take any such steps unless certain conditions and provisions set forth in Condition 9 (Events of Default and Enforcement) are satisfied.

Although the Trustee may institute such proceedings against the Issuer as it may think fit to enforce any obligation, condition or provision relating to the Notes binding on the Issuer under the Conditions (other than any payment obligations of the Issuer arising from the Notes or the Trust Deed including, without limitation, payment of principal or interest in respect of the Notes and any damages awarded for breach of obligations), the Issuer shall not, as a consequence of any such proceeding, be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.

Meetings of Noteholders; modification, waivers and substitution

Condition 13 (*Meetings of Noteholders, Modification and Waiver*) contains provisions for calling meetings of Noteholders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all Noteholders including Noteholders who do not attend and vote at the relevant meeting and/or Noteholders who vote in a manner contrary to the relevant majority.

In addition, the Trustee may, without the consent of Noteholders, agree to (i) any modification or waiver of, or authorisation of any breach or proposed breach of, the provisions of the Notes or (ii) the substitution of the Holding Company of the Issuer, a Successor in Business or any Subsidiary of the Issuer (each as defined in the Trust Deed) as principal debtor under the Notes in place of the Issuer, in each case in the circumstances described in Condition 15 (*Substitution*).

Because the Global Notes are held by or on behalf of Euroclear and Clearstream, Luxembourg, investors will have to rely on their procedures for transfer, payment and communication with the Issuer

The Notes will be represented by the Global Certificate except in certain limited circumstances described in the Global Certificate. The Global Certificate will be registered in the name of The Bank of New York Depository (Nominees) Limited as nominee for, and deposited with, the common depositary for Euroclear and Clearstream, Luxembourg. Note Certificates in definitive form evidencing holdings of Notes will only be available in certain limited circumstances. Euroclear and Clearstream, Luxembourg will maintain records of the beneficial interests in the Global Note Certificate. While the Notes are represented by the Global Certificate, investors will be able to trade their beneficial interests in the Notes only through Euroclear and Clearstream, Luxembourg.

While the Notes are represented by the Global Certificate, the Issuer will discharge its payment obligations under the Notes by making payments to or to the order of the common depositary for Euroclear and Clearstream, Luxembourg for distribution to their account holders. A holder of a beneficial interest in the Global Certificate must rely on the procedures of Euroclear and Clearstream, Luxembourg to receive payments under the Notes. The Issuer has no responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Certificate.

In order to exercise the voting rights attaching to the Notes, holders of beneficial interests in the Global Certificate will be required to comply with the procedures of Euroclear and Clearstream, Luxembourg.

Interest rate risks

Investment in the Notes involves the risk that subsequent changes in market interest rates may adversely affect the value of the Notes. In particular, investment in securities which pay a fixed rate of interest involve the risk that if market interest rates subsequently increase above the rate paid on such securities, this can be expected to adversely affect the market price of such securities.

The interest rate on the Notes will reset on 1 July 2020

The Notes will initially bear interest at the rate of 8.5 per cent. per annum until (but excluding) the Reset Date (the "**Initial Interest Rate**"). On the Reset Date, the interest rate will be reset to the sum of the initial margin of 6.53 per cent. and the 5 Year Mid-Swap Rate falling two Business Days prior to the Reset Date (the "**Reset Interest Rate**").

The Reset Interest Rate could be less than the Initial Interest Rate and could affect the market value of an investment in the Notes.

Minimum Denomination

As the Notes have denominations consisting of the minimum denomination of £100,000 plus higher integral multiples of £1,000, it is possible that the Notes may be traded in amounts in excess of £100,000 that are not integral multiples of £100,000. In such case a Noteholder who, as a result of trading such amounts, holds a principal amount of less than the minimum denomination may not receive a definitive Note Certificate in respect of such holding (should Note Certificates in definitive form be printed) and would need to purchase a principal amount of Notes such that its holding amounts to the minimum denomination.

Change of law

The Terms and Conditions of the Notes will be based on English law in effect as at the Issue Date. No assurance can be given as to the impact of any possible judicial decision or change to English law or administrative practice after the date of the issue of the Notes.

U.S. Foreign Account Tax Compliance Withholding

Sections 1471 through 1474 of the U.S. Internal Revenue Code of 1986 (or "**FATCA**") impose a new reporting regime and, potentially, a 30 per cent. withholding tax with respect to (i) certain payments from sources within the United States, (ii) "foreign passthru payments" made to certain non-U.S. financial institutions that do not comply with this new reporting regime, and (iii) payments to certain investors that do not provide identification information with respect to interests issued by a participating non-U.S. financial institution. The United States has entered into an intergovernmental agreement regarding the implementation of FATCA with the United Kingdom (the "**IGA**"). Whilst the Notes are in global form and held within Euroclear Bank SA/NV and Clearstream Banking, société anonyme (together, the "**ICSDs**"), in all but the most remote circumstances, it is not expected that FATCA or the IGA will affect the amount of any payment received by the ICSDs. However, FATCA may affect payments made to custodians or intermediaries in the subsequent payment chain leading to the ultimate investor if any such custodian or intermediary generally is unable to receive payments free of FATCA withholding. It also may affect payment to any ultimate investor that is a financial institution that is not entitled to receive payments free of withholding under FATCA, or an ultimate investor that fails to provide its broker (or other custodian or intermediary from which it receives payment) with any information, forms, other documentation or consents that may be necessary for the payments to be made free of FATCA withholding. Investors should choose the custodians or intermediaries with care (to ensure each is compliant with FATCA or other laws or agreements related to FATCA) and provide each custodian or intermediary with any information, forms, other documentation or consents that may be necessary for such custodian or intermediary to make a payment free of FATCA withholding. Significant aspects of when and how FATCA will apply remain unclear, and no assurance can be given that withholding under FATCA will not become relevant with respect to payments made on or with respect to the Notes in the future. An investor should be aware that if any payments in relation to a Note were subject to withholding or deduction under FATCA, the Issuer will not have an obligation to pay any additional amounts in relation to such withholding or deduction. Investors should consult their own tax adviser to obtain a more detailed explanation of FATCA and how FATCA may affect them. The Issuer's obligations under the Notes are discharged once it has made payment to, or to the order of, the common depositary for the ICSDs (as registered holder of the Notes) and the Issuer has therefore no responsibility for any amount thereafter transmitted through the ICSDs and custodians or intermediaries. Further, foreign financial institutions in a jurisdiction which has entered into an intergovernmental agreement with the United States (an "**IGA**") are generally not expected to be required to withhold under FATCA or an IGA (or any law implementing an IGA) from payments they make.

Withholding under the EU Savings Tax Directive

Under EC Council Directive 2003/48/EC on the taxation of savings income (the "**Savings Directive**"), each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria may instead apply a withholding system in relation to such payments, deducting tax at rates rising over time to 35 per cent. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments.

A number of non-EU countries including Switzerland, and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or, certain limited types of entity established in a Member State (a withholding system in the case of Switzerland). In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

The Council of the European Union formally adopted a Council Directive amending the Savings Directive on 24 March 2014 (the "**Amending Directive**"). The Amending Directive broadens the scope of the requirements described above. The Amending Directive requires Member States to apply these new requirements from 1 January 2017 and if they were to take effect the changes made under the Amending Directive would extend the scope of the Savings Directive to payments made to, or collected for, certain other entities and legal arrangements. They also broaden the definition of "interest payment" to cover income that is equivalent to interest.

However, the European Commission has proposed the repeal of the Savings Directive from 1 January 2017 in the case of Austria and from 1 January 2016 in the case of all other Member States (subject to ongoing requirements to fulfil administrative obligations such as the reporting and exchange of information relating to, and accounting for withholding taxes on, payments made before those dates). This is to prevent overlap between the Savings Directive and a new automatic exchange of information regime to be implemented under Council Directive 2011/16/EU on Administrative Co-operation in the field of Taxation (as amended by Council Directive 2014/107/EU). The proposal also provides that, if it proceeds, Member States will not be required to apply the new requirements of the Amending Directive.

Investors who are in any doubt as to their position should consult their professional advisers.

If a payment were to be made or collected through a Member State which has opted for a withholding system and an amount of, or in respect of, tax were to be withheld from that payment, neither the Issuer nor the Principal Paying Agent (as defined in the Terms and Conditions of the Notes) nor any other person would be obliged to pay additional amounts with respect to any Notes as a result of the imposition of such withholding tax. The Issuer is required to maintain an agent with a specified office in an EU Member State that will not be obliged to withhold or deduct tax pursuant to the Savings Directive or any law implementing or complying with, or introduced to confirm to, the Savings Directive.

TERMS AND CONDITIONS OF THE NOTES

The following is the text of the Conditions of the Notes which (subject to modification) will be endorsed on each Certificate issued in respect of the Notes:

The £250,000,000 Fixed Rate Reset Callable Subordinated Tier 2 Notes due 2025 (the **Notes**, which expression shall in these Conditions, unless the context otherwise requires, include any further notes issued pursuant to Condition 14 and forming a single series with the Notes) of The Co-operative Bank p.l.c. (the "**Issuer**") are constituted by a trust deed (such trust deed as modified and/or supplemented and/or restated from time to time, the "**Trust Deed**") dated on or around 1 July 2015 (the "**Issue Date**") and made between the Issuer and Law Debenture Trustees Limited (the "**Trustee**", which expression shall include its successor(s)) as trustee for the Noteholders (as defined below).

The statements in these Conditions include summaries of, and are subject to, the detailed provisions of and definitions in the Trust Deed. Copies of the Trust Deed, the agency agreement dated the Issue Date (such agency agreement as amended and/or supplemented and/or restated from time to time, the "**Agency Agreement**") made between the Issuer, the Trustee, The Bank of New York Mellon (Luxembourg) S.A., as registrar (the "**Registrar**", which expression shall include any successor registrar appointed from time to time), The Bank of New York Mellon, London Branch as principal paying agent (the "**Principal Paying Agent**", which expression shall include any successor principal paying agent appointed from time to time and, together with any additional paying agents appointed from time to time, the "**Paying Agents**") and the Calculation Agent (as defined herein) are available for inspection (by prior appointment) during normal business hours by the Noteholders at the registered office for the time being of the Trustee, being at the date of issue of the Notes at Fifth Floor, 100 Wood Street, London EC2V 7EX, United Kingdom. The Noteholders are entitled to the benefit of, are bound by, and are deemed to have notice of, all the provisions of the Trust Deed and the Agency Agreement applicable to them.

1. FORM, DENOMINATION AND TITLE

1.1 Form and Denomination

The Notes are issued in registered form in amounts of £100,000 and integral multiples of £1,000 in excess thereof (referred to as the "**principal amount**" of a Note). A note certificate (each a "**Certificate**") will be issued free of charge to each Noteholder in respect of its registered holding of Notes. Each Certificate will be numbered serially with an identifying number which will be recorded on the relevant Certificate and in the register of Noteholders which the Issuer will procure to be kept by the Registrar.

1.2 Title

Title to the Notes passes only by registration in the register of Noteholders. The holder of any Note will (except as otherwise required by law) be treated as its absolute owner for all purposes (whether or not it is overdue and regardless of any notice of ownership, trust or any interest or any writing on, or the theft or loss of, the Certificate issued in respect of it) and no person will be liable for so treating the holder. In these Conditions "**Noteholder**" and (in relation to a Note) "**holder**" means the person in whose name a Note is registered in the register of Noteholders (or, in the case of a joint holding, to the joint holder whose name appears first on the register of Noteholders in respect of such joint holding (the "**representative joint Noteholder**")).

2. TRANSFER OF NOTES AND ISSUE OF CERTIFICATES

2.1 Transfers

A Note may, subject to the Conditions below, be transferred by depositing the Certificate issued in respect of that Note, with the form of transfer duly completed and signed, at the specified office of the Registrar.

2.2 Delivery of new Certificates

Each new Certificate to be issued upon transfer of Notes will, within five business days of receipt by the Registrar of the duly completed form of transfer together with a valid Certificate, be mailed by uninsured mail at the risk of the holder entitled to the Note to the address specified in

the form of transfer. For the purposes of this Condition, "**business day**" shall mean a day on which banks are open for business in the city in which the specified office of the Registrar with whom a Certificate is deposited in connection with a transfer is located.

Where some but not all of the Notes in respect of which a Certificate is issued are to be transferred, a new Certificate in respect of the Notes not so transferred will, within five business days of receipt by the Registrar of the original Certificate, be mailed by uninsured mail at the risk of the holder of the Notes not so transferred to the address of such holder appearing on the register of Noteholders or as specified in the form of transfer.

2.3 **Formalities free of charge**

Registration of transfer of Notes will be effected without charge by or on behalf of the Issuer or the Registrar but upon payment (or the giving of such indemnity as the Issuer or the Registrar may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

2.4 **Closed Periods**

No Noteholder may require the transfer of a Note to be registered during the period of 15 days ending on the due date for any payment of principal or interest on that Note.

2.5 **Regulations**

All transfers of Notes and entries on the register of Noteholders will be made subject to the detailed regulations concerning transfer of Notes scheduled to the Trust Deed. The regulations may be changed by the Issuer with the prior written approval of the Registrar and the Trustee. A copy of the current regulations will be mailed (free of charge) by the Registrar to any Noteholder who requests one.

3. **STATUS AND SUBORDINATION OF THE NOTES**

3.1 **Status**

The Notes are unsecured and, in accordance with Condition 3.2, subordinated obligations of the Issuer and rank *pari passu* without any preference among themselves.

3.2 **Subordination**

On a winding-up of the Issuer, claims against the Issuer in respect of or arising under the Notes (including any damages awarded for breach of any obligations in respect of the Notes) will be subordinated in the manner provided in the Trust Deed to the claims of all Senior Creditors (as defined below) but shall rank:

(a) at least *pari passu* with all claims of holders of all other subordinated obligations of the Issuer which constitute, and all claims relating to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which constitute, or (in either case) would but for any applicable limitation on the amount of such capital constitute, Tier 2 Capital and all obligations which rank, or are expressed to rank, *pari passu* therewith ("**Parity Securities**"); and

(b) in priority to the claims of holders of:

(i) all obligations of the Issuer which rank or are expressed to rank, and all claims relating to a guarantee or other like or similar undertaking or arrangement given or undertaken by the Issuer in respect of any obligations of any other person which rank or are expressed to rank, junior to the claims in respect of the Notes, including (without limitation) obligations which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 1 Capital and all obligations which rank, or are expressed to rank, *pari passu* therewith; and

(ii) all classes of share capital of the Issuer,

(together, the "**Junior Securities**").

In these Conditions:

"**Senior Creditors**" means (i) depositors and other unsubordinated creditors of the Issuer; and (ii) subordinated creditors of the Issuer other than those whose claims rank, or are expressed to rank, *pari passu* with or junior to the claims of the holders of the Notes;

"**Tier 1 Capital**" and "**Tier 2 Capital**" have the respective meanings given to such terms in the Applicable Banking Regulations from time to time;

"**Applicable Banking Regulations**" means at any time the laws, regulations, requirements, guidelines and policies relating to capital adequacy then in effect in the United Kingdom (or in such other jurisdiction in which the Issuer may be organised or domiciled) and applicable to the Issuer, including, without limitation to the generality of the foregoing, those regulations, requirements, guidelines and policies relating to capital adequacy then in effect of the Relevant Authority and/or any regulation, directive or other binding rules, standards or decisions adopted by the institutions of the European Union; and

"**Relevant Authority**" means the Prudential Regulation Authority or such other authority (whether in the United Kingdom or elsewhere) having primary responsibility for prudential supervision of the Issuer.

3.3 **Set-Off**

Subject to applicable law, neither any Noteholder nor the Trustee may exercise or claim any right of set-off in respect of any amount owed to it by the Issuer arising under or in connection with the Notes and each Noteholder shall, by virtue of its subscription, purchase or holding of any Note, be deemed to have waived all such rights of set-off.

4. **INTEREST**

4.1 **Interest and Interest Payment Dates**

The Notes bear interest on their outstanding principal amount from and including the Issue Date at the applicable Interest Rate in accordance with the provisions of this Condition 4. Interest shall be payable annually in arrear on 1 July in each year from (and including) 1 July 2016 up to (and including) the Maturity Date (each an "**Interest Payment Date**").

4.2 **Interest Accrual**

Each Note will cease to bear interest from and including its due date for redemption unless, upon due surrender of the relevant Certificate, payment of the principal due in respect of the Note is improperly withheld or refused or unless default is otherwise made in respect of payment, in which event interest shall continue to accrue as provided in the Trust Deed.

4.3 **Calculation of Interest**

Interest shall be calculated on the basis of (i) the actual number of days in the period from and including the date from which interest begins to accrue (the "**Accrual Date**") to but excluding the date on which it falls due divided by (ii) the actual number of days from and including the Accrual Date to but excluding the next following Interest Payment Date (the "**Day Count Fraction**").

Interest shall be calculated per £1,000 in principal amount of the Notes. Accordingly, the amount of interest payable in respect of a Note for a relevant period shall be calculated by (i) multiplying the Day Count Fraction by the product of £1,000 and the applicable Interest Rate, (ii) rounding the resultant figure to the nearest £0.01 (£0.005 being rounded upwards) and (iii) multiplying that rounded figure by a fraction the numerator of which is the principal amount of such Note and the denominator of which is £1,000.

4.4 **Initial Interest Rate and Reset Interest Rate**

Interest will accrue:

(a) at 8.5 per cent. per annum (the "**Initial Interest Rate**") from (and including) the Issue Date to (but excluding) 1 July 2020 (the "**Reset Date**"); and

(b) thereafter at the Reset Interest Rate,

and references in these Conditions to the "**applicable Interest Rate**" shall be construed accordingly.

The amount of interest payable on each Interest Payment Date up to (and including) the Reset Date will be £85 per £1,000 in principal amount of Notes.

The "**Reset Interest Rate**" shall be the sum of the 5 Year Mid-Swap Rate (as determined by the Calculation Agent on the date (the "**Reset Determination Date**") falling two Business Days prior to the Reset Date) and the initial margin of 6.53 per cent., converted by the Calculation Agent from a semi-annual to an annual basis in a commercially reasonable manner, where:

"**5 Year Mid-Swap Rate**" means:

(i) the semi-annual mid-swap rate with a term of five years which appears on the Screen Page as of 11:00 a.m. (London time) on the Reset Determination Date; or

(ii) if such rate does not appear on the Screen Page at such time, the Reset Reference Bank Rate on the Reset Determination Date;

"**5 Year Mid-Swap Rate Quotations**" means the arithmetic mean of the bid and ask rates for the semi-annual fixed leg (calculated on an Actual/365 (Fixed) day count basis) of a fixed-for-floating Sterling interest rate swap which:

(i) has a term of five years commencing on the Reset Date;

(ii) is in an amount that is representative of a single transaction in the relevant market at the relevant time with an acknowledged dealer of good credit in the swap market; and

(iii) has a floating leg based on 6-month LIBOR rate (calculated on an Actual/365 (Fixed) day count basis);

"**Calculation Agent**" means The Bank of New York Mellon, London Branch (or any alternative or successor calculation agent appointed by the Issuer for this purpose);

"**Reset Reference Bank Rate**" means the percentage rate determined on the basis of the 5 Year Mid-Swap Rate Quotations provided by the Reset Reference Banks to the Calculation Agent at approximately 11:00 a.m. (London time) on the Reset Determination Date. If at least three quotations are provided, the Reset Reference Bank Rate will be the arithmetic mean of the quotations provided, eliminating the highest quotation (or, in the event of equality, one of the highest) and the lowest quotation (or, in the event of equality, one of the lowest). If only two quotations are provided, the Reset Reference Bank Rate will be the arithmetic mean of the quotations provided. If only one quotation is provided, the Reset Reference Bank Rate will be the quotation provided and, if no quotations are provided, the Reset Reference Bank Rate will be 1.797 per cent.;

"**Reset Reference Banks**" means six leading swap dealers in the London interbank market (excluding the Calculation Agent or any of its affiliates) selected by the Calculation Agent in its discretion after consultation with the Issuer; and

"**Screen Page**" means Reuters screen "ISDAFIX4" or such other page as may replace it on Reuters or, as the case may be, on such other information service that may replace Reuters, in each case, as may be nominated by the person providing or sponsoring the information appearing there for the purpose of displaying rates comparable to the 5 Year Mid-Swap Rate.

4.5 **Determination and Notification of the Reset Interest Rate**

The Calculation Agent will, as soon as practicable after 11.00 a.m. (London time) on the Reset Determination Date, determine the Reset Interest Rate and shall promptly thereafter notify the same to the Issuer, the Paying Agents, the Trustee and any stock exchange on which the Notes are for the time being listed or admitted to trading. As soon as reasonably practicable thereafter (and in any event no later than the second Business Day following the Reset Date), the Calculation Agent shall cause notice of the Reset Interest Rate to be given to the Noteholders in accordance with Condition 12.

The Reset Interest Rate so notified may subsequently be amended (or appropriate alternative arrangements made by way of adjustment) in the event of a manifest error, and the amended Reset Interest Rate shall promptly thereafter be notified to the Issuer, the Paying Agents, the Trustee, any stock exchange on which the Notes are for the time being listed or admitted to trading and to the Noteholders in accordance with Condition 12.

4.6 **Determinations by Trustee; determinations binding**

The Trustee (or an agent appointed by it) shall, if the Calculation Agent does not for any reason determine the Reset Interest Rate in accordance with Condition 4.5, determine the Reset Interest Rate. In doing so, the Trustee (or its agent) shall (if and to the extent that, in its opinion, it can practicably do so) apply the foregoing provisions of this Condition 4, with any consequential amendments it considers necessary, and in all other respects it shall determine the Reset Interest Rate in such manner as it shall deem fair and reasonable in all the circumstances (having regard to the provisions of this Condition 4). Such determination shall be deemed to be a determination thereof by the Calculation Agent.

All notifications, determinations and calculations made or obtained by the Calculation Agent (or by the Trustee or its agent) for the purposes of this Condition 4 shall, in the absence of wilful default or manifest error, be binding on the Issuer, the Trustee, the Registrar, any Paying Agent and the Noteholders and (in the absence of bad faith) no liability to the Issuer or the Noteholders will attach to the Calculation Agent or the Trustee (or its agent) in connection with the exercise of any of their duties and discretions with respect to the Notes.

5. **PAYMENTS**

5.1 **Payments in respect of Notes**

All payments in respect of the Notes will be made by sterling cheque or warrant drawn on a bank or building society in the United Kingdom, posted no later than the relevant due date and made payable to the Noteholder (in the case of a joint holding of Notes, the representative joint Noteholder) appearing in the register of Noteholders in respect of the Note of which he is the holder at the close of business on the fifteenth day before the relevant due date (the "**Record Date**") at the addresses shown in the register of Noteholders on the Record Date. Payments of principal and payments of interest due otherwise than on an Interest Payment Date will only be made against surrender of the relevant Certificate at the specified office of the Registrar or any Paying Agent.

Upon application of a Noteholder (or in the case of a joint holding of Notes, the representative joint Noteholder) to the Registrar, in the form from time to time prescribed by the Registrar, not less than ten days before the due date for any payment in respect of his Notes, the payment may be made by transfer on the due date or, if the due date is not a Business Day, on the immediately following Business Day to a sterling account with a bank or building society in the United Kingdom.

5.2 **Payments subject to applicable laws**

Payments in respect of principal and interest on Notes are subject in all cases to (i) any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 7 and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the **Code**) or otherwise imposed pursuant to Sections 1471 through 1474 (inclusive) of the Code, any

regulations or agreements thereunder, any official interpretations thereof, or (without prejudice to the provisions of Condition 7) any law implementing an intergovernmental approach thereto.

5.3 **No commissions**

No commissions or expenses shall be charged by the Issuer, the Registrar or any Paying Agent to the Noteholders in respect of any payments made in accordance with this Condition.

5.4 **Payments on Business Days**

Where payment of any principal and/or interest is to be made by transfer to a registered account, payment instructions (for value the due date or, if that is not a Business Day (as defined below), for value the first following day which is a Business Day) will be initiated, and where payment is to be made by cheque, the cheque will be mailed, on the Business Day preceding the due date for payment or, in the case of a payment of principal or a payment of interest due otherwise than on an Interest Payment Date, if later, on the Business Day on which the relevant Certificate is surrendered at the specified office of the Registrar or any Paying Agent.

Noteholders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due if the due date is not a Business Day, if the Noteholder is late in surrendering its Certificate (if required to do so) or if a cheque mailed in accordance with this Condition arrives after the due date for payment.

In these Conditions, "**Business Day**" means a day (other than a Saturday or Sunday) on which commercial banks are open for business in London and (in the case of surrender or presentation of a Certificate only) in the place in which the Certificate is surrendered or presented.

5.5 **Partial payments**

If the amount of principal or interest which is due on the Notes is not paid in full, the Registrar will annotate the register of Noteholders with a record of the amount of principal or interest in fact paid.

5.6 **Interpretation of Principal and Interest**

Any reference in these Terms and Conditions to principal in respect of the Notes shall be deemed to include any additional amounts which may be payable with respect to principal under Condition 7 or pursuant to any undertakings given in addition thereto or in substitution therefor pursuant to the Trust Deed.

Any reference in these Terms and Conditions to interest in respect of the Notes shall be deemed to include any additional amounts which may be payable with respect to interest under Condition 7 or pursuant to any undertakings given in addition thereto or in substitution therefore pursuant to the Trust Deed.

6. **REDEMPTION AND PURCHASE**

6.1 **Redemption at Maturity**

Unless previously redeemed or purchased and cancelled as specified below, the Notes will be redeemed by the Issuer at their principal amount on 1 July 2025 (the "**Maturity Date**").

6.2 **Redemption on the Reset Date at the option of the Issuer**

The Issuer may, subject to Condition 6.7 and having given not less than 30 nor more than 60 days' notice to the Noteholders in accordance with Condition 12 (which notice shall be irrevocable), elect to redeem the Notes, in whole but not in part, on the Reset Date at an amount equal to their principal amount together with unpaid interest accrued to (but excluding) the Reset Date.

6.3 Redemption for Tax Reasons

Subject to Condition 6.7 below, the Notes may be redeemed at the option of the Issuer, in whole but not in part, at an amount equal to their principal amount together with unpaid interest accrued to (but excluding) the date of redemption, at any time on the Issuer giving not less than 30 nor more than 60 days' notice to the Noteholders (which notice shall be irrevocable), if the Issuer satisfies the Trustee immediately before the giving of the aforementioned notice that:

(a) on the occasion of the next payment due under the Notes, the Issuer has or will become obliged either to pay additional amounts as provided or referred to in Condition 7 or to account to any taxing authority in the Tax Jurisdiction for any amount (other than tax withheld or deducted from interest payable on such Notes) in respect of such payment in each case as a result of any change in or amendment to (including a prospective change in or amendment to) the laws or regulations of the Tax Jurisdiction or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after the Issue Date; or

(b) interest payments under or with respect to the Notes are no longer fully deductible for UK corporation tax purposes as a result of any change in or amendment to (including a prospective change in or amendment to) the laws or regulations of the Tax Jurisdiction or any change in the application or official interpretation of such laws or regulations, which change or amendment becomes effective on or after the Issue Date,

and (in either case) such obligation cannot be avoided by the Issuer taking reasonable measures available to it (each a "**Tax Event**"), provided that no such notice of redemption shall be given earlier than 90 days prior to (in the case of (a) above) the earliest date on which the Issuer would be obliged to pay such additional amounts or make a payment in respect of which it would be obliged to account to any taxing authority as aforesaid were a payment in respect of the Notes then due or (in the case of (b) above) the start of the accounting period of the Issuer in which interest payments on the Notes would cease to be so deductible.

"**Tax Jurisdiction**" means the United Kingdom or any political subdivision or any authority thereof or therein having power to tax.

Prior to the publication of any notice of redemption pursuant to this Condition 6.3, the Issuer shall deliver to the Trustee, to make available for inspection (by prior appointment) at its specified office to the Noteholders, (i) a certificate signed by two Directors of the Issuer stating that the Issuer is entitled to effect such redemption and setting forth a statement of facts showing that the conditions precedent to the right of the Issuer so to redeem have occurred, and (ii) an opinion of independent legal or tax advisers of recognised standing to the effect either that such a circumstance does exist or that, upon a change in or amendment to the laws (including any regulations thereunder) or in the interpretation or administration thereof, of the Tax Jurisdiction which at the date of such certificate is proposed to be made and in the opinion of such independent legal or tax advisers and the Issuer (based on such opinion) is reasonably expected to become effective on or prior to the date when the relevant payment in respect of such Notes would otherwise be made, becoming so effective, such circumstances would exist.

The Trustee shall be entitled to accept and rely upon the certificate as sufficient evidence of the satisfaction of the conditions precedent set out above, in which event it shall be conclusive and binding on the Noteholders.

6.4 Regulatory Event Redemption

Subject to Condition 6.7 below, the Notes may be redeemed at the option of the Issuer, in whole but not in part, at an amount equal to their principal amount together with unpaid interest accrued to (but excluding) the date of redemption, at any time on the Issuer giving not less than 30 nor more than 60 days' notice to the Noteholders (which notice shall be irrevocable), if, at any time after the Issue Date, the Issuer determines that as a result of a change (or pending change which the Relevant Authority considers to be sufficiently certain) in the regulatory classification of the Notes under the Applicable Banking Regulations, the entire principal amount of the Notes fully ceases (or would be likely to fully cease) to qualify as Tier 2 Capital of the Issuer (whether on an

individual or a consolidated basis) for the purposes of Applicable Banking Regulations (a "**Regulatory Event**").

6.5 **Purchases**

Subject to Condition 6.7 below, the Issuer or any of its subsidiaries may at any time purchase or otherwise acquire any of the outstanding Notes at any price in the open market or otherwise. Such Notes may be held, reissued, resold or, at the option of the Issuer, surrendered to the Registrar or any Paying Agent for cancellation.

6.6 **Cancellation**

All Notes which are redeemed, and any Notes which are purchased and surrendered for cancellation pursuant to Condition 6.5, shall be immediately cancelled and cannot be reissued or resold.

6.7 **Redemption and Purchase Conditions**

The Issuer shall not be permitted to redeem or purchase the Notes prior to the Maturity Date unless the following conditions (in each case, if and to the extent then required by Applicable Banking Regulations) are satisfied:

(a) the Issuer has given any requisite notice to the Relevant Authority and has obtained the Relevant Authority's prior permission to the redemption or purchase (as the case may be) of the Notes;

(b) in the case of any redemption of Notes prior to the fifth anniversary of the Issue Date upon the occurrence of a Tax Event or a Regulatory Event, the Issuer has demonstrated to the satisfaction of the Relevant Authority (i) that the circumstances giving rise to the Tax Event or, as the case may be, the Regulatory Event were not reasonably foreseeable as at the Issue Date and, (ii) in the case of a Tax Event only, that the change in the applicable tax treatment is material or, in the case of a Regulatory Event only, that the change in the applicable regulatory classification is sufficiently certain; and

(c) any redemption or purchase of the Notes must be carried out in accordance with the Applicable Banking Regulations.

7. **TAXATION**

All payments of principal and interest in respect of the Notes by or on behalf of the Issuer will be made without withholding or deduction for or on account of any present or future taxes, duties, assessments or governmental charges of whatever nature imposed or levied by or on behalf of the Tax Jurisdiction (as defined in Condition 6.3), unless such withholding or deduction is required by law. In such event, the Issuer will pay such additional amounts as shall be necessary in order that the net amounts received by the holders of the Notes after such withholding or deduction shall equal the respective amounts of principal and interest which would otherwise have been receivable in respect of the Notes, in the absence of such withholding or deduction, except that no such additional amounts shall be payable with respect to any Note:

(a) the holder of which is liable for such taxes or duties in respect of such Note by reason of its having some connection with the Tax Jurisdiction other than the mere holding of such Note; or

(b) presented for payment (where presentation is required) more than 30 days after the Relevant Date (as defined below) except to the extent that the holder thereof would have been entitled to an additional amount on presenting the same for payment on such thirtieth day; or

(c) presented for payment (where presentation is required) in the United Kingdom; or

(d) where such withholding or deduction is imposed on a payment to an individual and is required to be made pursuant to European Council Directive 2003/48/EC on the taxation

of savings income or any law implementing or complying with, or introduced in order to conform to, such Directive; or

(e) presented for payment (where presentation is required) by or on behalf of a Noteholder who would have been able to avoid such withholding or deduction by presenting the relevant Note to another Paying Agent in a Member State of the European Union.

As used herein, the "**Relevant Date**" means the date on which such payment first becomes due, except that, if the full amount of the moneys payable has not been duly received by the Principal Paying Agent or the Trustee on or prior to such due date, it means the date on which, the full amount of such moneys having been so received, notice to that effect is duly given to the Noteholders in accordance with Condition 12.

8. PRESCRIPTION

Claims in respect of principal and interest will become void unless made within a period of ten years (in the case of principal) and five years (in the case of interest) after the Relevant Date (as defined in Condition 7) therefor.

9. EVENTS OF DEFAULT AND ENFORCEMENT

9.1 If default is made in the payment of any principal or interest due on the Notes or any of them on the due date and such default continues in the case of principal for a period of 7 days and in the case of interest for a period of 15 days, the Trustee may, subject as provided below, at its discretion and without further notice, institute proceedings for the winding-up of the Issuer, but may take no other action in respect of such default.

9.2 If, otherwise than for the purposes of a reconstruction or amalgamation on terms previously approved in writing by the Trustee, an order is made or an effective resolution is passed for winding-up the Issuer, the Trustee may, and, if so requested in writing by the holders of at least one-fifth in nominal amount of the Notes then outstanding or if so directed by an Extraordinary Resolution (as defined in the Trust Deed) of the holders of the Notes shall (subject in each case to being indemnified and/or secured and/or pre-funded to its satisfaction), give notice to the Issuer that the Notes are, and they shall thereby become, immediately due and repayable at their principal amount, together with accrued interest as provided in the Trust Deed. In such event the Trustee shall be entitled to prove in the winding-up of the Issuer and shall have no other remedy against the Issuer.

9.3 Without prejudice to Condition 9.1, if the Issuer fails to perform, observe or comply with any obligation, condition or provision relating to the Notes binding on it under these Conditions (other than any payment obligations of the Issuer arising from the Notes or the Trust Deed including, without limitation, payment of principal or interest in respect of the Notes and any damages awarded for breach of obligations) the Trustee may, subject as provided below, at its discretion and without further notice, institute such proceedings against the Issuer as it may think fit to enforce such obligation, condition or provision provided that the Issuer shall not as a consequence of such proceeding be obliged to pay any sum or sums sooner than the same would otherwise have been payable by it.

9.4 The Trustee shall not be bound to take the action referred to in Condition 9.1 or Condition 9.3 unless (i) it shall have been so directed by an Extraordinary Resolution of the Noteholders or so requested in writing by the holders of at least one-fifth in nominal amount of the Notes outstanding and (ii) it shall have been indemnified and/or secured and/or pre-funded to its satisfaction.

9.5 No remedy against the Issuer, other than the institution of proceedings by the Trustee for the winding-up of the Issuer and/or proving in the winding-up of the Issuer, shall be available to the Trustee or the Noteholders for the recovery of amounts owing in respect of the Notes as aforesaid (including damages awarded for breach of any obligations) and no holder of a Note shall be entitled to institute proceedings for the winding-up of the Issuer or to prove in such winding-up unless the Trustee, having become bound so to proceed in accordance with Condition 9.4, fails to

do so or fails to prove in such winding-up, in each case within a reasonable time and such failure shall be continuing.

10. REPLACEMENT OF CERTIFICATES

Should any Certificate be lost, stolen, mutilated, defaced or destroyed, it may be replaced at the specified office of the Registrar upon payment by the claimant of such costs and expenses as may be incurred in connection therewith and on such terms as to evidence and indemnity as the Issuer may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

11. REGISTRAR AND PAYING AGENTS

The names of the initial Registrar and Principal Paying Agent and their initial specified offices are set out below.

The Issuer is, with the prior written approval of the Trustee, entitled to vary or terminate the appointment of the Registrar and/or the Principal Paying Agent and/or appoint additional or other Registrars and/or Paying Agents and/or approve any change in the specified office through which any Registrar and/or Paying Agent acts, provided that:

(a) so long as the Notes are listed on any stock exchange, there will at all times be a Paying Agent with a specified office in such place as may be required by the rules and regulations of the relevant stock exchange (or any other relevant authority);

(b) there will at all times be a Paying Agent with a specified office in a European city (which may be London) approved in writing by the Trustee;

(c) there will at all times be a Paying Agent and a Registrar; and

(d) there will at all times be a Paying Agent in a European Union Member State (if any) that is not obliged to withhold or deduct tax pursuant to European Council Directive 2003/48/EC or any law implementing or complying with, or introduced in order to conform to, such Directive.

Notice of any termination or appointment and of any changes in specified offices will be given to the Noteholders promptly by the Issuer in accordance with Condition 12.

In acting under the Agency Agreement, subject as provided therein, the Registrar and the Paying Agents will act solely as agents of the Issuer, and will not assume any obligations or relationships of agency or trust to or with the Noteholders, except that (without affecting the obligations of the Issuer to the Noteholders to repay the Notes and to pay interest thereon) funds received by the Paying Agents for the payment of any sums due in respect of the Notes shall be held by them on behalf of the Noteholders until the expiry of the relevant period of prescription under Condition 8. The Agency Agreement contains provisions for the indemnification of the Registrar and the Paying Agents.

12. NOTICES

All notices to the Noteholders will be valid if mailed to them at their respective addresses in the register of Noteholders maintained by the Registrar. The Issuer shall also ensure that notices are duly given or published in a manner which complies with the rules and regulations of any stock exchange or other relevant authority on which the Notes are for the time being listed. Any notice shall be deemed to have been given on the second day after being so mailed or on the date of publication or, if so published more than once or on different dates, on the date of the first publication.

13. MEETINGS OF NOTEHOLDERS, MODIFICATION AND WAIVER

13.1 Meetings of Noteholders

The Trust Deed contains provisions for convening meetings of the Noteholders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of the Notes or certain provisions of the Trust Deed. Such a meeting may be convened by the Issuer, the Trustee or by Noteholders holding not less than 10 per cent. in nominal amount of the Notes for the time being remaining outstanding. The quorum at any such meeting for passing an Extraordinary Resolution is one or more persons holding or representing a clear majority in nominal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons being or representing Noteholders whatever the nominal amount of the Notes so held or represented, except that at any meeting the business of which includes the modification of certain provisions of the Notes (including modifying the date of maturity of the Notes or any date for payment of interest thereon, reducing or cancelling the amount of principal or the rate of interest payable in respect of the Notes or altering the currency of payment of the Notes) or certain of the provisions of the Trust Deed, the necessary quorum for passing an Extraordinary Resolution will be one or more persons holding or representing not less than two-thirds, or at any adjourned such meeting not less than one-third, in nominal amount of the Notes for the time being outstanding. An Extraordinary Resolution passed at any meeting of the Noteholders shall be binding on all the Noteholders, whether or not they are present at the meeting.

13.2 Modification and Waiver

The Trust Deed provides that the Trustee may agree, without the consent of the Noteholders, to any modification (subject to certain exceptions as provided in the Trust Deed) of, or to any waiver or authorisation of any breach or proposed breach of, any of these Terms and Conditions or any of the provisions of the Trust Deed, or may determine that any condition, event or act which, but for such determination, would constitute an event giving rise to the right of the Trustee described in Condition 9, shall not be treated as such which in any such case, in the opinion of the Trustee, is not materially prejudicial to the interests of the Noteholders or to any modification of any of these Terms and Conditions or any of the provisions of the Trust Deed or the Agency Agreement which is, in the opinion of the Trustee, of a formal, minor or technical nature, which is made to correct a manifest error or which, in the opinion of the Trustee, is not materially prejudicial to the interests of Noteholders. Any such modification, waiver, authorisation or determination shall be binding on the Noteholders and, unless the Trustee agrees otherwise, any such modification shall be notified to the Noteholders as soon as practicable thereafter in accordance with Condition 12.

13.3 Rights of Trustee

In connection with the exercise by it of any of its trusts, powers, authorities or discretions (including, but without limitation, any modification, waiver, authorisation or substitution), the Trustee shall have regard to the interests of the Noteholders as a class and, in particular, but without limitation, shall not have regard to the consequences of such exercise for individual Noteholders resulting from their being for any purpose domiciled or resident in, or otherwise connected with, or subject to the jurisdiction of, any particular territory and the Trustee shall not be entitled to require, nor shall any Noteholder be entitled to claim, from the Issuer or any other person any indemnification or payment in respect of any tax consequence of any such exercise upon individual Noteholders except to the extent already provided for in Condition 7 and/or any undertaking given in addition to, or in substitution for, Condition 7 pursuant to the Trust Deed.

13.4 Compliance with Applicable Banking Regulations

The Issuer shall comply with Applicable Banking Regulations in connection with any modification or proposed modification of these Terms and Conditions.

14. FURTHER ISSUES

The Issuer shall be at liberty from time to time without the consent of the Noteholders to create and issue further notes having terms and conditions the same as the Notes or the same in all respects save for the amount and date of the first payment of interest thereon and so that the same shall be consolidated and form a single series with the outstanding Notes.

15. SUBSTITUTION

The Trustee may, without the consent of the Noteholders, agree with the Issuer to the substitution in place of the Issuer (or of any previous substitute under this Condition) as the principal debtor under the Notes and the Trust Deed of the Holding Company of the Issuer, a Successor in Business or any Subsidiary of the Issuer (each as defined in the Trust Deed), subject to (i) in the case of a substitution of any Subsidiary of the Issuer, the Notes being unconditionally and irrevocably guaranteed by the Issuer and so that the obligations of the Issuer under such guarantee shall be subordinated on a basis considered by the Trustee to be equivalent to that in respect of the Issuer's obligations in respect of the Notes, (ii) the Trustee being satisfied that the interests of the Noteholders will not be materially prejudiced by the substitution, (iii) the obligations of such Holding Company of the Issuer or Successor in Business or, in the case of substitution of a Subsidiary of the Issuer, the obligations of the Subsidiary and of the Issuer under its guarantee, being subordinated on a basis considered by the Trustee to be equivalent to that in respect of the Issuer's obligations as principal debtor in respect of the Notes, and (iv) certain other conditions set out in the Trust Deed being complied with. In making any such determination of equivalence of subordination for the purposes of paragraphs (i) and (iii) above, the Trustee shall be entitled to request that the Issuer, and the Issuer shall be obliged to, procure an opinion of independent legal advisers of recognised standing and the Trustee shall be entitled to accept the provision of and rely upon such opinion in satisfaction of its making such determination.

The Issuer shall comply with Applicable Banking Regulations in connection with any substitution of the Issuer (or any previous substitute) under this Condition.

16. INDEMNIFICATION OF THE TRUSTEE

The Trust Deed contains provisions for the indemnification of the Trustee and for its relief from responsibility in certain circumstances including provisions relieving it from instituting proceedings to enforce repayment or exercise any powers, duties, authorities or discretions unless indemnified and/or secured and/or pre-funded to its satisfaction.

The Trustee may rely without liability to Noteholders on a report, confirmation or certificate or any advice or any accountants, financial advisers, financial institution or any other expert, whether or not addressed to it and whether their liability in relation thereto is limited (by its terms or by any engagement letter relating thereto entered into by the Trustee or in any other manner) by reference to a monetary cap, methodology or otherwise. The Trustee may accept and shall be entitled to rely on any such report, confirmation or certificate or advice and such report, confirmation or certificate or advice shall be binding on the Issuer, the Trustee and the Noteholders.

The Trustee is not responsible for monitoring or supervising the performance by the Registrar, the Paying Agents and/or any other person of its obligations to the Issuer and may assume these are being performed unless and until it has actual knowledge to the contrary.

17. CONTRACTS (RIGHTS OF THIRD PARTIES) ACT 1999

No rights are conferred on any person under the Contracts (Rights of Third Parties) Act 1999 to enforce any term of this Note, but this does not affect any right or remedy of any person which exists or is available apart from that Act.

18. GOVERNING LAW

The Trust Deed, the Agency Agreement, the Notes and any non-contractual obligations arising out of or in connection with the Trust Deed, the Agency Agreement and the Notes are governed by, and shall be construed in accordance with, English law.

SUMMARY OF PROVISIONS RELATING TO THE NOTES IN GLOBAL FORM

The Notes will initially be represented by a Global Certificate that will be registered in the name of The Bank of New York Mellon Depository (Nominees) Limited as nominee for, and deposited with, a common depositary for Euroclear and Clearstream, Luxembourg.

The Global Certificate will contain provisions that modify the Terms and Conditions of the Notes as they apply to the Notes evidenced by the Global Certificate, and a summary of certain of those provisions is set out below:

Exchange for definitive Note Certificates

Registration of title to Notes in a name other than that of The Bank of New York Depository (Nominees) Limited (or any replacement or successor nominee for Euroclear and Clearstream, Luxembourg) will be permitted only if both Euroclear and Clearstream, Luxembourg are closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or announce an intention permanently to cease business or do in fact do so and no alternative clearing system satisfactory to the Trustee is available.

Thereupon, the holder of the Global Certificate (acting on the instructions of one or more of the Accountholders) may give notice to the Issuer of its intention to exchange the Global Certificate for definitive Note Certificates on or after the Exchange Date (as defined below).

On or after the Exchange Date, the registered holder may surrender the Global Certificate to or to the order of the Registrar. In exchange for the Global Certificate, the Registrar will deliver, or procure the delivery of, definitive Note Certificates printed in accordance with any applicable legal and stock exchange requirements and in or substantially in the form set out in the Trust Deed. On exchange of the Global Certificate, the Issuer will procure that it is cancelled and, if the registered holder so requests, returned to the registered holder together with any relevant definitive Note Certificates.

For these purposes, "**Exchange Date**" means a day specified in the notice requiring exchange falling not less than 10 days after that on which such notice is given and being a day on which banks are open for general business in the place in which the specified office of the Registrar is located.

Subject as provided in the following paragraph, until the exchange of the whole of the Global Certificate as aforesaid, the registered holder thereof shall in all respects be entitled to the same benefits as if it were the registered holder of definitive Note Certificates, representing the Notes for the time being represented by the Global Certificate.

Accountholder

For so long as all of the Notes are represented by the Global Certificate and such Global Certificate is held on behalf of Euroclear and/or Clearstream, Luxembourg, each person who is for the time being shown in the records of Euroclear or Clearstream, Luxembourg as the holder of a particular principal amount of such Notes (each an "**Accountholder**") (in which regard any certificate or other document issued by Euroclear or Clearstream, Luxembourg as to the principal amount of such Notes standing to the account of any person shall, in the absence of manifest error, be conclusive and binding for all purposes) shall be treated as the holder of such principal amount of such Notes for all purposes (including for the purposes of any quorum requirements of, or the right to demand a poll at, meetings of the Noteholders) other than with respect to the payment of principal and interest on such Notes, the right to which shall be vested, as against the Issuer and the Trustee, solely in the registered holder of the Global Certificate in accordance with and subject to its terms and the terms of the Trust Deed.

Transfers

Book-entry interests in the Notes represented by the Global Certificate are transferable only in accordance with, and subject to, the provisions hereof and the rules and operating procedures of Euroclear and Clearstream, Luxembourg. Transfers of such book-entry interests will be effected through the records of Euroclear and Clearstream, Luxembourg and their respective direct and indirect participants in accordance with the rules and procedures of Euroclear and Clearstream, Luxembourg and their respective direct and indirect participants.

Payments

Payments due in respect of Notes represented by the Global Certificate shall be made to or to the order of the registered holder and such payment will discharge the obligations of the Issuer in respect of the relevant payment under the Notes. Each Accountholder must look solely to Euroclear or Clearstream, Luxembourg as the case may be, for its share of each payment made to or to the order of the registered holder.

Notices

For so long as all of the Notes are represented by the Global Certificate and the Global Certificate is held on behalf of Euroclear and/or Clearstream, Luxembourg, notices to Noteholders may be given by delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg (as the case may be) for communication to the relative accountholders rather than by publication as required by Condition 12 (*Notices*) provided that, so long as the Notes are admitted to listing or trading on any stock exchange, such notice is also given in a manner which complies with the rules and regulations of such stock exchange or other relevant authority. Any such notice shall be deemed to have been given to the Noteholders on the second day after the day on which such notice is delivered to Euroclear and/or Clearstream, Luxembourg (as the case may be) as aforesaid.

Record Date

For so long as all Notes are held in Euroclear and Clearstream, Luxembourg, the Record Date shall be determined in accordance with Condition 5.1 (*Payments in respect of Notes*) provided that the words "fifteenth day" shall be deemed to be replaced with "ICSD Business Day". "**ICSD Business Day**" means a day on which the Clearing Systems are open for business.

Calculation of interest

For so long as all of the Notes outstanding are represented by the Global Certificate, interest will be calculated in respect of the aggregate principal amount of the Notes represented by the Global Certificate (and not per £1,000 in principal amount of Notes as provided in Condition 4.3 (*Calculation of Interest*)) but otherwise in accordance with Condition 4 (*Interest*).

Prescription

Claims against the Issuer in respect of principal and interest on the Notes represented by the Global Certificate will become void after 10 years (in the case of principal) and five years (in the case of interest) from the Relevant Date (as defined in Condition 7 (*Taxation*)) therefor.

Clearing Systems

References in the Global Certificate and in this Prospectus to Euroclear and/or Clearstream, Luxembourg shall be deemed to include references to any other clearing system approved by the Trustee.

USE OF PROCEEDS

The issue of the Notes is a part of the approximately £400 million of additional capital not regarded as CET1 capital that the revised business plan (as accepted by the PRA) envisages that the Bank will raise, which is expected to be completed during the early stages of the planning period, and, once issued, will help the Bank to comply with FCA and PRA regulatory requirements and expectations in further strengthening the Bank's regulatory capital base. In addition, the net proceeds received by the Bank will be used by the Bank for general corporate purposes.

DESCRIPTION OF THE BANK

1. OVERVIEW

The Bank was originally formed as the banking department of the Co-operative Wholesale Society Limited ("**CWS**") in 1872. CWS changed its name on 14 January 2001 to Co-operative Group (CWS) Limited. Co-operative Group (CWS) Limited changed its name to Co-operative Group Limited ("**Co-operative Group**") following the merger with United Co-operatives Limited on 29 July 2007.

The Bank as a separate legal entity was incorporated as The Co-operative Bank Limited in October 1970. In July 1971, the business formerly carried on by the banking department of Co-operative Group was transferred to and vested in the Bank. This was followed, in June 1973, by the transfer of the business of the banking department of the former Scottish Co-operative Wholesale Society to the Bank.

The Bank obtained clearing bank status in 1975 and was granted recognised status by the Bank of England under the terms of the Banking Act 1979. In 1981, the Bank re-registered under the Companies Act 1980 as a public company and was re-registered on 10 January 1993 with its present name. On 19 June 2002, Co-operative Group transferred its entire shareholding in the Bank to Co-operative Financial Services Limited (now named Co-operative Banking Group Limited ("**CBG**")), a newly incorporated Industrial and Provident Society. The ultimate parent of the Bank remained Co-operative Group.

The Bank merged with Britannia Building Society ("**Britannia**") on 1 August 2009 (the "**Merger**"). As at the date of this document, the retail residential lending and savings franchise transferred from Britannia and the pre-Merger businesses of the Bank, continue to trade as separate businesses under the "Britannia", "Co-operative Bank" and "smile" brand names respectively.

Following a review of the Bank's capital position in 2013, it was concluded that the Bank required an additional £1.5 billion of aggregate CET1 capital. To meet the capital shortfall, Co-operative Group and the Bank embarked on a recapitalisation plan (the "**Recapitalisation Plan**") which included the following:

(i) A liability management exercise (the "**Liability Management Exercise**") aimed at generating around £1.2 billion of new CET1 capital, which was completed on 20 December 2013. The Liability Management Exercise involved: (i) the issuance of £0.2 billion of new subordinated debt and £0.6 billion of new ordinary shares in exchange for £1.3 billion of existing debt and preference shares and additional contributions from bondholders of £0.1 billion; (ii) the cancellation of £0.4 billion of existing ordinary share capital which resulted in the creation of a capital redemption reserve of the same value; and (iii) the sale of investment assets that were used as economic hedges for the existing debt, generating a profit of £11 million;

(ii) A commitment of the CBG to contribute £333 million of CET1 capital by the end of 2014; and

(iii) £40 million of CET1 capital being generated in 2014 from interest savings on the securities surrendered in the Liability Management Exercise.

A further £400 million, before costs, of CET1 capital, was raised in May 2014 through the issue of new ordinary shares (the "**Capital Raising**").

In December 2014, the PRA announced the results of the Bank of England stress tests and confirmed that the Bank's capital resources were projected to be exhausted in the Bank of England's hypothetical stress scenario and therefore the Bank did not meet the requirements of the stress test scenario. As a result, the Bank was required to submit a revised business plan to demonstrate that it could deliver the level of resilience required for a bank of its planned future size and business model to withstand the stress test scenario by the end of the planning period (2015 to 2019). This revised business plan was accepted by the PRA. A key source of vulnerability in the stress scenario, relating to a severe housing-related stress scenario, stems

from the Bank's Non-core Business and in particular, the Optimum residential portfolio of loans. For further information, please refer to the risk factor entitled "*A failure to successfully implement or a delay in implementing the Bank's strategy may adversely impact the Bank's business, operating results, financial condition and prospects, its regulatory capital position and its ability to comply with its regulatory capital requirements*".

The Bank's revised business plan, which runs from 2015 to 2019 does not change the Bank's overarching strategy, but it does look to accelerate the deleveraging of the Non-core Business, and in particular, the Optimum residential mortgage portfolio of loans, with a view to significantly improving the Bank's resilience to a stress test as severe as the one run by the Bank of England in 2014, towards the end of the revised business plan and maintaining the required capital ratios under the aforementioned stress by that time. On 6 May 2015, the Bank successfully closed its inaugural whole capital structure securitisation of approximately £1.5 billion comprising part of its non-core residential mortgage portfolio, Optimum through Warwick Finance One.

The Bank's long-term senior unsecured debt is currently rated Caa2 (rating under review for possible downgrade) by Moody's, and B (negative outlook) by Fitch, which ratings are below investment grade.

2. STRATEGY

The Bank is split into two business areas: the Core Business and the Non-core Business. The Bank's overarching strategy, which involves a turnaround plan of approximately four-to-five years, is to leverage its brand strength and high levels of customer satisfaction to create, over time, an efficient and profitable bank with a reduced overall risk profile. The Bank aims to focus its Core Business on retail banking and SME customers where the Bank considers it has strong existing market credentials, customer relationships and expertise. Those assets which are not consistent with the Bank's business strategy and classified as part of the Non-core Business will be actively managed to achieve the most appropriate asset value on an individual or portfolio basis. In line with this strategy, the Bank has deleveraged a part of the Optimum portfolio of residential mortgage loans as described in "*Description of the Bank – 1. Overview*" above and paragraph 3(C.3)(a) below.

3. BUSINESS OVERVIEW

Following the equity capital raisings by the Bank as part of the Liability Management Exercise and the Capital Raising, the Bank's ordinary shares as at 30 April 2015 were:

(a) 20.16 per cent. owned by the Co-operative Group (which holds its interest through CBG); and

(b) 79.84 per cent. owned by other shareholders, including each of the following which have notable holdings: Silver Point 12.57 per cent., Perry Capital 9.19 per cent., York Capital 8.28 per cent. and Invesco Asset Management 7.44 per cent. See also "*Material Shareholdings*" below.

The Co-operative Group is therefore an associate and a related party of the Bank. See also "*Material Shareholdings*" below.

A. The Core Business and the Non-core Business

As part of the Bank's plan to simplify and reshape itself, its strategy focuses on the following business activities:

(i) Lines of business that are consistent with the Bank's strategy and risk appetite (the "**Core Business**"): Retail ("**Retail Banking**"); core business and commercial banking business ("**BACB**") and treasury ("**Treasury/other**"); and

(ii) Asset classes which are not consistent with the Bank's business strategy and are managed for run down or exit (the "**Non-core Business**"): Co-operative Asset Management.

As at 31 December 2014, total segment assets in the Core Business and Non-core Business were £25,476.2 million and £10,753.0 million, respectively.

B. Core Business

The Core Business is split into three business areas: (i) Retail Banking; (ii) BACB; and (iii) Treasury/other, as described below.

B.1 Core Business: Retail Banking

Retail Banking offers a range of financial products and services to individuals and households throughout the UK, trading as "The Co-operative Bank", "Britannia" and "smile" together with the Bank's intermediary brand "Platform".

The Bank has approximately 4.3 million Retail Banking customers and is a clearing bank operating across multiple delivery channels with a range of current accounts and money transmission services, lending products and savings products. The Bank distributes its retail products through branches, call centres and via the internet and mobile banking. See paragraph (c) titled "*Distribution*" below for further details on the distribution of products.

As part of its business strategy, the Bank intends to introduce new products that are simple, transparent on fees and interest charged and fairly priced.

(a) ***Retail Banking Products***

(i) **Mortgage lending**

As at 31 December 2014, the retail Bank had a total outstanding mortgage portfolio of £11.2 billion issued under the Co-operative Bank brand and the Britannia brand and a total outstanding mortgage portfolio of £2.4 billion issued under the Platform brand. As at 31 December 2014, the Bank's total issued mortgage lending secured on residential property (excluding buy-to-let) was £12.6 billion and the total issued buy-to-let mortgage portfolio was £1.0 billion. The Bank's total mortgage lending of £11.2 billion represents an estimated 0.91 per cent. of total UK mortgage balances (as at 31 December 2014).

During the twelve months ended 31 December 2014, the Bank's gross new lending amounted to £1.1 billion (which includes further advances) and net new lending was negative at £1.9 billion.

(ii) **Unsecured lending**

The unsecured lending products offered by the Bank consist of personal unsecured loans, credit cards and overdraft facilities.

Personal unsecured loans

The majority of the Bank's personal unsecured lending portfolio comprises fixed rate lending either to customers who have an existing relationship with the Bank (classified as personal loans) or to customers with no broader relationship with the Bank (classified as direct loans). The Bank has now exited the direct loans market so the Bank's new personal unsecured lending business is presently to customers holding an existing relationship with the Bank.

Credit cards

The Bank had 503,896 credit card accounts of which 344,021 were active during the month of December 2014 (in that the relevant account recorded a debit or a credit during that month being sufficient to constitute activity for these purposes).

The Bank markets and processes credit card applications itself (using its credit scoring system), and credit card holders receive differing credit limits, depending on their credit score. Credit limits are regularly reviewed in line with customer need and risk appetite.

Overdrafts

Overdrafts are offered to customers with current accounts with the Bank. In line with peers in the market, the Bank offers two types of overdraft; formal overdrafts and informal overdrafts. Formal overdrafts are where an overdraft is requested by the customer and agreed to in writing by the Bank.

Informal overdrafts are where a customer pays or withdraws money from their account, either in excess of their credit balance where no formal overdraft has been agreed or in excess of their overdraft limit where it has been agreed. Formal overdraft facilities are reviewed each year.

(iii) **Savings and current accounts**

As at 31 December 2014, the Bank had 651,214 primary current accounts (being accounts that on average turnover £800 or more per month) and £25.6 billion of retail customer deposit balances, representing an estimated 1.97 per cent. of total UK retail savings balances. The Bank offers a range of savings products and current accounts. The Bank offers a standard Current Account and a Current Account Plus, as well as a basic current account, called Cashminder directed at simple, in-credit banking and a book of historic packaged/fee-paying current accounts which are not presently part of the Bank's on-sale product range.

The Bank offers a range of savings products including term, limited access and easy access products, with or without an individual savings account ("**ISA**") wrapper. The Bank's fixed rate savings accounts earn a fixed rate of interest for a chosen term and funds therein cannot be withdrawn until maturity.

The Bank's strategy is to simplify the range of current accounts and savings products with price varying by term, access and amount whilst addressing the needs of target customers. The Bank intends to migrate from expensive fixed-term deposits to variable rate funding. A compelling current account proposition with enhanced digital capability is planned to appeal to target customers.

(b) ***Distribution***

Overview

The Bank offers a broad multi-channel proposition to customers, covering branch, telephone, online, mobile and intermediary/broker (through Platform).

Distribution strategy

Over the medium term, the Bank's strategy is to move towards a more digitally enabled offering that is less branch intensive, and facilitates broader customer self-service options for the Bank's customers' everyday transactional needs, whilst retaining the richness of the branch proposition to support customers with complex needs. In this future distribution model, it is intended that:

- the remote channels (internet and digital), which currently have limited functionality, will become the primary point of contact for the Bank's customers looking for information on their account, simple product queries, simple transactions and simple sales;
- the Bank's call centres will support the digital channels (e.g. webchat) via callback facilities and appointment booking, cater for more complex queries (such as complaints) and provide emergency support, as well as providing

simple transaction services and information to customers for whom digital is not an option;

- the Bank's branch network will provide face-to-face support for customers and, as a secondary role, help customers use the Bank's digital services and provide simple transaction services and information to customers for whom digital is not an option; and

- there will be continued usage of intermediaries for mortgages.

B.2 Core Business: BACB

BACB targets and services small and medium sized businesses which will typically (i) have a turnover of less than £25 million; (ii) have borrowing requirements of less than £10 million; and (iii) otherwise meet the Bank's risk appetite. BACB also offers services on commercial terms, to charities, social businesses and co-operatives.

B.3 Core Business: Treasury/other

The core responsibilities for the Bank's Treasury department are to ensure a strong and stable liquidity base, provide diverse sources of wholesale funding to the Bank, manage market risk within risk appetite and deliver a strong financial performance on the investment portfolio. "Other" comprises Unity Trust Bank, a subsidiary bank operating in the corporate banking and social economy sectors on behalf of trade unions. On 14 January 2014, it was announced that the Bank is in discussions with the board of Unity Trust Bank about a potential sale of the Bank's 26.7 per cent. shareholding. Discussions continue but remain at an early stage and any decision on a changed ownership structure would be subject to regulatory approval.

C. Non-core Business

The Non-core Business consists of asset classes of the Bank that are not consistent with the Bank's Core Business strategy. In July 2013, Co-operative Asset Management ("**CoAM**") was established by the Bank to oversee proactive management, disposal and run-off of these non-core asset classes in accordance with CoAM's strategic objective (the "**Non-core Assets**"). CoAM is the successor to the Bank's legacy corporate and business banking non-core segment (part of which used to be designated in the old core business) which was established in 2012. CoAM contains a significant part of the Bank's impairment risk.

C.1 CoAM

Funding

The Non-core Business is predominantly funded by deposits from the Core Business. It is also funded by deposits from the Non-core Business and by securitisation transactions.

C.2 Non-core Assets

The Non-core Assets are identified on the basis of the following criteria:

assets which cannot be supported by the Bank's Core Business retail platform. These include assets which are (i) corporate assets where the borrower typically has a turnover in excess of £25 million; (ii) customers that require more complex banking support for transactions (eg guarantees or letters of credit); or (iii) not consistent with the Bank’s risk appetite;

- assets which fail to deliver a positive net interest margin for the Bank including liquidity costs and/or a return on capital above the cost of capital or;

- non-performing or defaulting assets (excluding those assets under the BACB segment of the Core Business).

The Non-core Assets comprise of asset classes with total outstanding loans of £10.7 billion as at 31 December 2014. This is a mixture of revolving credit facilities and stage drawdown facilities

primarily in the Corporates, Renewable Energy and Asset Finance ("**REAF**"), Private Finance Initiative ("**PFI**") and Commercial Real Estate ("**CRE**") portfolios. In the period from 31 December 2013 to 31 December 2014, £2.4 billion of Non-core Assets (consisting of Non- core Business loans) were deleveraged, through a combination of asset sales, run-off and managed repayments, net of new drawdowns.

C.3 Non-core Asset Classes

(a) ***Optimum***

Optimum was created following the merger with Britannia and is a closed book of non-prime intermediary and acquired mortgage book assets including non-prime residential mortgages (both income verified and self-certified), buy-to-let and other non-conforming mortgages. The Optimum gross customer balances as at 31 December 2014 stood at £6.8 billion.

Following the 2014 Bank of England hypothetical stress testing result, the Bank re-phased and revised its strategic plan to accelerate the de-leveraging of the Optimum portfolio. As part of the revised business plan, on 6 May 2015, the Bank successfully closed its inaugural, full capital structure securitisation of approximately £1.5 billion of Non-core Assets comprising a part of the Optimum residential mortgage portfolio, to assist with the accelerated deleveraging of the Optimum residential mortgage portfolio. The Bank purchased 65 per cent. of the class A notes (being a principal amount of £707,200,000) issued by Warwick Finance One in order to manage its liquidity position.

(b) ***Corporates***

Corporates is a £1.2 billion portfolio made up of leveraged, syndicated and relationship connections.

(c) ***CoAM CRE***

As at 31 December 2014, this portfolio had net loans of £1.2 billion.

The strategy for the non-performing part of this portfolio is to analyse, identify, restructure if necessary and execute exit options on a case-by-case basis.

(d) ***Project Finance Initiatives and Project Finance***

This is a £1.0 billion portfolio (as at 31 December 2014) of predominantly low margin, long-dated loans to finance public private partnership, project finance initiatives, such as schools, universities and hospitals and roads.

(e) ***Housing Association***

This is a £0.8 billion portfolio (as at 31 December 2014) across long-dated (average life of 20 years), predominantly low margin and high credit quality assets.

(f) ***Renewable Energy and Asset Finance***

This is a £0.4 billion portfolio (as at 31 December 2014) of specialised energy lending, mainly relating to wind farms, as well as combined heat and power and hydro.

As at 31 December 2014, the portfolio had gross loans of £444.11 million.

In December 2014 the Bank announced that it had entered into a conditional sale agreement for the disposal of a portion of the REAF portfolio to L1 Renewables Limited, a wholly owned subsidiary of Universities Superannuation Scheme Limited. The final disposal portfolio will be selected at completion, from a gross pool with a par value of approximately £323 million for a cash sum.

4. INFORMATION TECHNOLOGY ("IT")

The Bank's IT systems support a range of functions related to the delivery of its products and services. As a result of historical underinvestment (amongst other factors), the Bank's digital offerings significantly lag behind its competitors and a number of the Bank's IT systems now, or will soon, require both hardware and operating systems to be refreshed. The existing IT systems have a number of known resilience-related risks (which are under active management), which fall broadly into the categories of: disaster recovery, design of IT systems and single points of failure, end of life technology and third party suppliers. There are also issues with the Bank's ability to quickly launch new products on its platform. Since 2013, the Bank has undertaken a review of its overall IT requirements and has agreed a new IT development plan which is to be executed in phases and has been designed to meet the requirements of the Core Business strategy of the Bank.

The Bank will be required to make significant levels of IT related investment to make its platform fit-for-purpose resilient and provide the minimum levels of functionality required by the strategy. These investments may contribute to cost savings eventually but they are primarily about improved resilience. As a result, significant costs are expected to be incurred over the next one to three years. In parallel to the enhancement of the core platform, the Bank shall continue to support its non-core operations, which may, whilst it deleverages its Non-core Assets, impact its ability to drive savings from the rationalisation of its IT systems.

In January 2015 the Bank announced it had entered into a contract with IBM to migrate its IT infrastructure from the Co-operative Group into IBM-managed data centres and receive a full suite of managed services. A summary of the IBM arrangement can be found below (see paragraph 9 entitled *"Material Contracts"* below).

The majority of the Bank's software application is supported by a third party, Steria Limited ("**Steria**") (which is currently contracted via CFSMS). The Bank also uses Steria for application development and project management.

Security

The security of the Bank's IT systems is an area of importance, with an internal team responsible for all IT security build-and-run activities. The Bank invested in security technologies during 2013 and 2014, investing in identity and access management, firewall refresh, security monitoring and addressing legacy security infrastructure. These phased programmes of work will continue into 2015 and beyond and aim to address critical risks, including strengthening the internal IT security team and aligning policy and supporting controls to industry standards e.g. ISO27001 and PCI-DSS.

The Bank is working towards full compliance with the Payment Card Industry Data Security Standard, which is a common set of security standards developed by the major card providers to ensure that payment card data is processed, stored and transmitted securely.

Business Continuity

As indicated previously, the Bank's infrastructure is in need of an upgrade in numerous respects. Across the Bank's IT infrastructure there are varying levels of resilience and recoverability and whilst a basic level of resilience to a component-level failure is in place, the Bank does not currently have a proven end-to-end disaster recovery capability, especially in the case of a mainframe failure or a significant data centre outage.

The migration of IT infrastructure to an IBM platform (announced on 23 January 2015) is expected to deliver proven end-to-end disaster recovery capability by the end of 2016.

The Bank has received written confirmation from the FCA that the Bank not having a proven end-to-end disaster recovery capability constitutes a breach of the FCA Threshold Conditions. The FCA is closely supervising the Bank as it works towards restoring compliance with COND 2.4 of the FCA Threshold Conditions as they relate to non-financial resources. The FCA is not currently proposing further immediate supervisory intervention or the immediate exercise of any additional regulatory powers as a result of this assessment. The FCA reserves the right to take action in the future in relation to this breach. The PRA's general policy is not to communicate its

assessment of its position in relation to the PRA threshold conditions. The threshold conditions for which the PRA is responsible in relation to the Bank are set out in paragraphs 5A to 5F of Part 1E of Schedule 6 of the FSMA. However, both the PRA and FCA are closely monitoring the position of the Bank and the Bank remains in continual dialogue with both regulators.

5. SEPARATION

Prior to the Liability Management Exercise, certain functions of the Bank were centralised and carried out by the Co-operative Group. There are currently two key arrangements in place pursuant to which the Bank receives the supply of services, assets and/or personnel:

Project Unity

Between 2011 and 2013 the Bank transferred a number of functions and a substantial number of personnel to the Co-operative Group and entered into arrangements pursuant to which the Co-operative Group would provide certain services to the Bank. This project is known within the Bank as "Project Unity" ("**Project Unity**"). In connection with Project Unity, the Co-operative Group, CFSMS (an indirect subsidiary of the Co-operative Group) and the Bank entered into two key agreements relating to (i) the provision by the Co-operative Group of certain IT services to the Bank (the "**IT Services Agreement**"); and (ii) a number of individual service contracts for the provision of certain other services by the Co-operative Group to the Bank pursuant to a Professional Services Master Services Agreement (the "**Professional Services Master Services Agreement**" or "**PSMSA**").

CFSMS Arrangements

References to "**CFSMS Arrangements**" or the "**2006 Agreement**" relate to arrangements between CFSMS and the Bank regarding the provision of services, personnel and on-supply of certain third party services and assets to the Bank dating from 2006. CFSMS was established as a direct 100 per cent. subsidiary of CBG in 2005, to enable economies of scale through the sharing of employees and sourcing of third party services across CBG, including the Bank, CIS General Insurance Limited, Co-operative Insurance Society Limited, The Co-operative Asset Management Limited and later, Reclaim Fund Limited.

Separation Principles

On 4 November 2013, the Bank and the Co-operative Group agreed certain high level principles (the "**Separation Principles**") to govern future discussions between the Bank and the Co-operative Group regarding the separation arrangements between the Bank and the Co-operative Group. The parties intend to document any arrangements to resolve certain separation matters in a manner consistent with the Separation Principles. The Separation Principles include an overarching agreement to act in good faith and, amongst other things:

- A commitment that, until appropriate alternative arrangements for Project Unity and the CFSMS Arrangements are agreed, the Co-operative Group will continue to provide services to the Bank under the same terms that such services are currently provided.

- For those costs allocated by Co-operative Group in its sole discretion, the Bank and Co-operative Group will take reasonable steps to avoid the Bank incurring costs incremental to those it currently incurs.

- The Co-operative Group and the Bank will mitigate costs arising for Co-operative Group or the Bank from (i) Co-operative Group being a less than 50 per cent. shareholder of the Bank or (ii) agreed steps taken in connection with the separation process (acknowledging that the Bank shall be under no obligation to accept the transfer of any assets or liabilities that are not wholly or predominantly related to the continuing business of the Bank).

- Costs will be allocated between the Bank and Co-operative Group on an equitable basis.

- A working group consisting of representatives from the Bank and Co-operative Group will be established to address and oversee the separation work-stream.

Consistent with the Separation Principles, Co-operative Group and the Bank have also agreed the following basis on which Project Unity and the CFSMS Arrangements will be unwound:

(a) ***Project Unity***

(i) *Back to Bank*

The scope of services to be provided under the existing IT Services Agreement and the Professional Services Master Services Agreement will be reduced such that the significant majority of these services will either be taken back into the Bank or replacement suppliers appointed under new arrangements.

(ii) *Interim arrangements*

The Bank and the Co-operative Group entered into an IT Separation Costs Agreement on 22 January 2015. In consequence of this agreement and the Bank's IT outsourcing agreement with IBM for enterprise computing services, the Bank is not progressing the proposed revised IT Service Agreement and Professional Services Master Services Agreement which were described in the 2014 Annual Report. For further information, please refer to "*Material Contracts"* below.

(iii) *Costs*

The Bank has recognised a provision of £112.3 million (2013: £39.4 million) in relation to separation costs.

(b) ***CFSMS Arrangements***

(i) *Interim arrangements*

The Bank and CFSMS agreed that:

- CFSMS will establish a small dedicated management team to deal with contract management following CBG's disposal of insurance subsidiaries; and
- the CFSMS management team will manage CFSMS' supplies to the Bank (comprising services seconded employees, and third party services and assets) to ensure these meet the requirements of the current agreement between CFSMS and the Bank.

(ii) *Costs*

Costs will be allocated between the Bank and The Co-operative Group on an equitable basis.

(c) ***IT Separation Costs Agreement***

This agreement is described in more detail under *Material Contracts*.

6. MATERIAL SHAREHOLDINGS

As at 30 April 2015 (the latest practicable date prior to the date of this Prospectus), so far as is known to the Bank, the name of each person who, directly or indirectly, is interested in 5 per cent. or more of the Bank's share capital, and the amount of such person's interest is as follows:

Name	Share type	Number of shares held	Percentage
Co-operative Group Limited[(1)]	Preference	60,000,000	100
Co-operative Banking Group	Ordinary	90,994,303	20.16
SP Coop Investment, Ltd. (Cayman)	Ordinary	56,743,734	12.57
Perry Capital	Ordinary	41,498,709	9.19

Name	Share type	Number of shares held	Percentage
Goldentree	Ordinary	39,874,988	8.83
York Capital	Ordinary	37,368,184	8.28
Invesco	Ordinary	33,581,426	7.44
Strategic Value Partners	Ordinary	23,806,208	5.27

(1) In connection with the Liability Management Exercise, The Co-operative Group Limited signed a deed of waiver waiving any rights to income and capital in respect of the preference shares.

7. RECENT DEVELOPMENTS IN CAPITAL ADEQUACY

During 2013 and 2014, the Bank was able to improve its capital position and reduce its overall risk profile as a result of the Liability Management Exercise, planned capital injections from the CBG and ongoing deleveraging. £400 million of additional capital being raised in May 2014 through the Capital Raising and the CBG CET1 injections of £333 million throughout 2014 were the primary factors in the Bank's CET1 position increasing by £0.56 billion between December 2013 and December 2014. The increase in CET1 has resulted in the Bank's fully-loaded CRD IV CET1 ratio increasing by 5.8 per cent., from 7.2 per cent. as at 31 December 2013 to 13.0 per cent. as at 31 December 2014.

The Bank's risk weighted assets decreased by £2.5 billion during 2014 from £15.1 billion to £12.6 billion and there has been a reduction of £1.4 billion in the Bank's Non-core risk weighted assets from £8.6 billion to £7.2 billion. The Bank's leverage ratio was 4.3 per cent as at 31 December 2014, which is an increase of 1.9 per cent. since the 2013 year end.

For most of 2014 the Bank was not compliant with its Individual Capital Guidance ("**ICG**"), being the PRA's statement as to the regulatory capital it expects the Bank to hold. On 31 December 2014, the final injection of the aggregate one-off £333 million contribution from CBG, as part of the Recapitalisation Plan, helped push the Bank into ICG compliance, however due to the Bank's ongoing losses, this position should be regarded as a temporary situation. The Bank met the Pillar 1 capital requirement throughout the year ended 31 December 2014.

The revised business plan, which has been accepted by the PRA, anticipates the Bank will meet the minimum 7 per cent. CET1 ratio throughout the planning period (2015 to 2019) and the 4.5 per cent. CET1 ratio under stress by the end of 2019. The revised business plan anticipates sustainably meeting ICG by the latter part of the planning period, and compliance with its CPB is not anticipated until the end of the planning period. See the risk factor entitled "*The Bank's business, operating results, financial condition and prospects and/or its ability to implement its strategy may be adversely impacted by it not maintaining adequate regulatory capital, by future changes to its regulatory capital requirements and by changes to PRA expectations in respect of capital adequacy*".

8. LITIGATION AND ARBITRATION

The following regulatory investigations and enquiries are in progress:

8.1 *Consumer Credit Act 1974*

In compliance with the CCA, the Bank is obliged to send loan account customers annual statements and notices of sums in arrears ("**NOSIAs**"). Those documents must be sent at specific times and must also comply with the information requirements for such documents which are contained within the CCA's associated regulations. The Bank failed to comply with some of its obligations under the CCA (in relation to both its secured and unsecured books).

The consequence of the Bank failing to comply with those obligations is that impacted customers are not liable to pay interest and default fees from a date specified by the CCA until (a) the account closes; or (b) the failure to comply with the obligations under the CCA is remedied (if the account is open).

The Bank is currently in the process of a redress and remediation programme to ensure that all impacted (and open) customer accounts are remedied in accordance with the provisions of the CCA and all customers whose accounts are now closed receive sufficient financial redress.

The Bank no longer offers CCA secured loans.

A provision of £169.4 million (2013: £109.5 million) has been recognised as at 31 December 2014 in respect of the total expected cost to the Bank for potential customer redress relating to the above alleged failings.

As at the date of this prospectus it is not possible for the Bank to confirm that additional CCA breaches will not be uncovered moving forward which could impact the financial position of the Bank. As impacted customers are not liable to pay interest and default fees, income on these loans will continue to not accrue until the accounts are remediated.

8.2 ***PPI***

Provisions have been made in respect of potential customer compensation claims relating to past sales of PPI. Claims are investigated on an individual basis and, where appropriate, compensation payments are made. For a number of years, the Bank, along with many other financial services providers, sold PPI alongside mortgage and non-mortgage credit products. The Bank stopped selling non-mortgage PPI in January 2009 and stopped selling mortgage PPI in March 2012. However, products still exist within the Bank which will include an element of PPI from historic sales.

The Financial Services Authority (the prudential and conduct regulator preceding the PRA and FCA) (the "**FSA**") issued a policy statement in August 2010 which amended the 'Disputes Resolution: Complaints' section of the Financial Services Handbook, setting out new rules for handling complaints, including complaints of PPI mis-selling. The Bank must comply with the policy statement which requires complainants to receive adequate redress and the Bank to complete a proactive review of all past business to identify mis-sold policies where no complaint has been made.

On 4 January 2013, the FSA fined the Bank £113,300 for failing to handle PPI complaints fairly during the period 21 January 2011 and 9 May 2011. During this period, the British Bankers Association unsuccessfully challenged the FSA measures (published in August 2010) designed to ensure all PPI complaints are treated fairly. The FSA found that during this period it was likely the Bank unfairly put on hold a significant proportion of 1,629 complaints, incorrectly deciding that they could not be determined because the outcome of the judicial review would have a bearing on the final decision.

In November 2014, the Supreme Court handed down a decision in *Plevin v Paragon Personal Finance Ltd* [2014] UKSC 61. The decision concerns the disclosure of commission amounts received in respect of sales of single premium PPI. In line with the rest of the banking industry and the Financial Ombudsman Service, the Bank is considering the implications of the judgement on both current and prior claims made concerning both single and repeat premium PPI. The decision has a potential impact on the number of the Bank's customers who may have a claim for PPI mis-selling and the treatment of prior claims. However, the Bank is not currently able to determine if it will need to make additional provisions in relation to the judgement. There is a risk, depending on the interpretation and application of the judgement that the Bank, in line with the banking industry in general, may need to make additional provisions for PPI.

An additional provision of £103.0 million for redress relating to PPI has been recognised in the period 1 January 2013 to 31 December 2013 and a further £5 million recognised in the period 1 January 2014 to 31 December 2014 increasing the total cost of carrying out work and paying compensation to £352.0 million (2013: £347 million). The provision raised in the Bank's 2014 financial statements is based on the FSA's (as it was then known) policy statement and industry claims experience, and on the published views and requirements of the FCA (which, for the avoidance of doubt, are not specific to the Bank). Any change in the FCA's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, could have a material adverse impact on the financial condition of the Bank and there is a risk of greater scrutiny and/or further regulatory action from the FCA.

This provision represents management's current estimate of the anticipated costs of related customer contact and redress, including administration expenses. Its calculation requires

significant judgement by management in determining appropriate assumptions, which include the level of complaints, uphold rates, proactive contact and response rates, and Financial Ombudsman Service referral and uphold rates.

8.3 ***Interest rate hedging products ("IRHPs") mis-selling claims***

The Bank sold IRHPs to certain SME (non-sophisticated) customers.

On 29 June 2012, the FSA (as it was then known) announced the results of its thematic review of IRHP sales. The review found serious failings in the sale of such products by Barclays Bank PLC, HSBC Bank plc, Lloyds Bank plc and the Royal Bank of Scotland plc to non-sophisticated customers. The FSA agreed to a past business review (PBR) and redress exercise with these banks.

On 11 July 2012 the Bank volunteered to participate in the past business review ("**PBR**") and redress those non-sophisticated customers which had been mis-sold IRHPS (the "**IRH PBR**").

The Bank's IRH PBR is on-going and involves an assessment of historic interest rate hedging product sales against eight sales standards (as agreed in collaboration with the FCA).

The Bank's PBR assesses whether each sale complied with the sale standards and where the Bank cannot document that it has adhered to the these standards, takes the opportunity to construct a redress proposal that places the customer back into the position they would have been in, had they had a fully compliant sale. The potential outcomes of the Bank's review of each sale in the PBR are:

(i) that the sale was fully compliant; (ii) that the sale was not fully compliant but that no redress is payable; or (iii) that the sale was not compliant and redress is due. Redress may involve inter alia switching the customer to an alternative product (which may or may not include payment of an amount representing the difference between payments made with the existing product and those which would have been made with the alternate product), or ripping up the existing IRHP and refunding payments made for the product. A provision of £14.8 million (2013: £33.0 million) for mis-selling has been recorded. The decrease in the provision from £33.0 million in 2013 to £14.8 million in 2014 reflects the utilisation of part of the opening provision in the period to date.

The Bank has conducted the PBR in accordance with the FCA guidance and under the supervision of the skilled person. The PBR appears to be in the latter stages, however there remains a risk until such time as the FCA concludes it is satisfied with the Bank's participation.

8.4 ***Third-Party card protection***

Between 1999 and 2012, the Bank introduced and/or sold third-party card and identity protection products to its customers through a number of different third parties. In July 2013, the FCA contacted the Bank directly, confirming that it considered one of the third party's product offering to be defective (as customers could receive certain elements of the protection provided for free from their bank) and suggested that the Bank may be expected, moving forward, to offer redress to customers as a consequence of such failings.

The Bank met with the FCA in September 2013 to discuss the FCA's concerns with the third-party product. Further to this meeting, the Bank received a circular letter from the FCA on 15 October 2013, giving reasons why the FCA considered that the Bank is liable, together with the third-party provider, to pay redress for sales of card protection products made between 14 January 2005 and 1 October 2012, and/or sold prior to 14 January 2005 and renewed before 1 October 2012. The Bank stopped actively advocating the third-party product in February 2012. The FCA asked that the Bank cooperate with the FCA in the implementation of a customer redress process.

The Bank has done so and is now participating within a time barred Scheme of Arrangement alongside the third party provider and a number of other UK banks / lenders (the "**Scheme**") which will be utilised to pay redress to customers.

As at the date of this Prospectus, it is difficult to estimate the final cost, of the redress process to the Bank, as it is unclear how many customers will claim under the Scheme, and because the Bank has minimal data on sales and renewals of the third-party product (such that it is difficult to make, even broad, assumptions). Whilst the exact nature and extent of any redress is not fully clear at this stage, a provision of £14.9 million (2013: £26.1 million) has been recognised as at 31 December 2014 in respect of the total expected cost to the Bank for potential customer redress relating to the above alleged failings.

8.5 ***Platform and Mortgage Agency Services First Payment***

The Bank has identified an issue related to the first payment made by a significant number of current and former mortgage customers in relation to their capital and interest (repayment) mortgages. The first monthly payment collected from borrowers was less than that stated in their "Offer Key Facts Illustration" document that they received because the capital element of the payment was not collected. This meant that the capital not collected attracted mortgage interest which was added to the account each subsequent month. It is believed that the issue affects all Platform advances, intermediary mortgage sales and all Mortgage Agency Services ("**MAS**") further advances completed between 1 January 1996 and 10 March 2013. A number of Platform advances and MAS further advances completed prior to 1996 are also affected.

The Bank raised a provision of £17.8 million (2013: £29.0 million) as at 31 December 2014 and is compensating customers.

8.6 ***Arrears Fees and Charges***

The Bank undertook a wide-ranging review of secured arrears fees across the various brands and products that exist with a view to aligning arrears fees charged across the Bank and verify compliance with the MCOB rules.

As a result of the review a revised fee structure was implemented in December 2013 and the Bank is in the process of undertaking a programme of work to verify that historic fees or charges were levied in accordance with the FCA's (previously the FSA's) MCOB rules.

The Bank has raised this issue, and continues to liaise, with the FCA. Based upon further work undertaken to refine the scope of its review the Bank has raised a provision of £34.8 million (2013: £19.0 million) as at 31 December 2014.

8.7 ***Early Repayment Charges Issue***

The Bank has also sold regulated mortgages containing early repayment charges ("**ERC**"). There are several regulatory requirements that regard both the features an ERC must have and the disclosure process that must be completed when offering a mortgage. The disclosure process requires specific documentation to be sent to the customer at the offer stage.

Failure to observe the regulatory requirements can make the ERC unenforceable and could lead to actions by regulators. ERCs can also be construed as penalties, where they do not represent a genuine pre-estimate of loss, or unfair terms, where they are not individually negotiated.

Where the Bank has failed to satisfy the relevant regulatory requirement, the ERC is deemed a penalty or the ERC is held to be an unfair term, it is possible that the Financial Ombudsman Service or the courts may order the Bank to refund any charge and pay compensation for any additional cost, distress or inconvenience.

The Bank has held a number of discussions with the FCA and a provision of £24 million (2013: £31 million) was made as at 31 December 2014.

8.8 ***Forbearance***

The Bank had proactively identified a potential risk of customer detriment from past practices of forbearance. A third-party review was undertaken to assess potential customer impact, which included a review of forbearance policies, data analysis and high-level file reviews.

Prior to the conclusion of the review the FCA published, on 25 February 2014, a Thematic Review on mortgage lenders arrears management and forbearance. The review sets out the FCA's findings into lenders' approaches and updates its expectations following its mortgage arrears and repossessions handling reviews in 2008 and 2009.

The Bank has initiated a redress programme in respect of various breaches of mortgage conduct of business rules. It is also the subject of a skilled persons review into potential detriment to its mortgage customers arising from, amongst other matters, arrears handling. The outcome of the review is uncertain but could potentially lead to enforcement investigations by the FCA.

Based on a further review, the Bank has reduced the original provision of £22 million in 2013 to £20m as at 31 December 2014.

8.9 ***Packaged current accounts***

The risks associated with the potential mis-sale of packaged current accounts is an industry-wide issue. There is increased scrutiny by regulatory bodies and there is a risk of increased numbers of complaints from customers and through claims management companies. The Bank has identified a limited number of issues relating to certain product features and groups of customers where it has concluded that redress is appropriate. As at 31 December 2014, a provision of £17.4 million was raised (2013: £0). The Bank continues to keep the wider position under review and there is a risk that further deficiencies may be identified. The Bank's approach to provisions for historic mis-selling of packaged current accounts is based on the views and requirements of the FCA. There remains a risk that any change in the FCA's current approach, such as an extension of the period covered by the requirement for proactive contact with customers, may result in greater scrutiny and/or further regulatory action from the FCA.

8.10 ***Other regulatory investigations***

The Bank is also subject to or involved in the following regulatory investigations and enquiries, including by (but not limited to):

- the PRA, which is undertaking an enforcement investigation in relation to the Bank and as part of that investigation will consider the role of former senior managers;

- the FCA, which is undertaking enforcement investigations covering decisions, events and processes at the Bank over the period from the Merger with Britannia to the end of 2013. These enforcement investigations carried out by the FCA and PRA began in January 2014 and have now been ongoing for 18 months. FCA and PRA have recently indicated that their preliminary view is that they are minded to make findings against the Bank covering certain decisions, events and processes over the period from mid-2008 to end 2013. Based on their current view, the FCA and PRA have indicated they intend to commence formal settlement discussions in July 2015. The outcome of any settlement discussions is currently uncertain both in the details of any findings and any potential financial penalty. No indication of the potential quantum of any financial penalty contemplated by FCA and PRA has yet been given to the Bank;

- HM Treasury, first announced in November 2013 and confirmed in March 2015 (following the publication of the Treasury Select Committee report into the Bank) that it would appoint a skilled person to review events at the Bank and the circumstances surrounding them from 2008, including the Verde transaction and the Merger with Britannia. The investigation will review the actions of relevant authorities (regulators and government) but will not commence until it is clear that it will not prejudice the outcome of the PRA and FCA investigations mentioned above; and

- the FRC, which launched an investigation under its Accountancy Scheme into the preparation, approval and audit of the Bank's accounts over the financial years 2009 – 2012. The focus of the FRC investigation is into the role of auditors or individual accountants rather than the Bank itself.

9. MATERIAL CONTRACTS

The following is a summary of contracts (not entered into in the ordinary course of the Bank's business) which could result in any member of the Bank's group being under an obligation or entitlement that is material to the Bank's ability to meet its obligations to Noteholders in respect of the Notes being issued.

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9.2 *2006 Agreement, the IT Services Agreement, the IT Separation Costs Agreement and Data Protection Agreement*

On 16 February 2006, the Bank and CFSMS entered into the 2006 Agreement in relation to the provision of shared IT assets and the on-supply of certain third party services by CSFMS. This is a cost-based agreement terminable by CFSMS on six months' notice with a 12-month run-off period. The Bank has no right to terminate unless CFSMS is subject to a change of control. The Bank provides CFSMS with an indemnity for all liabilities, losses, damages, costs and expenses of any nature as a result of CFSMS entering into and performing the agreement in respect of the assets, services and personnel provided to the Bank.

The Bank and the Co-operative Group entered into the IT Separation Costs Agreement on 22 January 2015, which then allowed the Bank to enter into an IT outsourcing agreement with IBM for enterprise computing services (which it entered into on 23 January 2015). Under the IT Separation Costs Agreement, both the Co-operative Group and CFSMS undertake to support activities for the separation of the Bank's IT infrastructure from the wider Co-operative Group's IT infrastructure, to enable the smooth transition to IBM. Further, the Co-operative Group undertakes that any notice to terminate the IT Services Agreement and CFSMS undertakes that any notice to terminate the 2006 Agreement would not take effect prior to 31 December 2017, to give the Bank sufficient time to separate the Bank’s IT infrastructure. The IT Separation Costs Agreement also allocated the contributions to be made towards the Co-operative Group's own costs of keeping the wider Co-operative Group's existing IT infrastructure stable and operable during and following the Bank's separation of its IT infrastructure; to this end CBG (as the parent of CFSMS) undertook to contribute a maximum of £95 million towards such Co-operative Group costs, with the Bank to make a contribution of up to £25 million, based on a formula in the event that the total cost of this Co-operative Group project falls between £76 million and £120 million.

The Bank and the Co-operative Group have negotiated the terms of a data processing agreement, which has three purposes:

(i) To create a legal obligation on both Bank and Co-operative Group to provide to each other, and to each other’s subcontractors, the data that is necessary to complete Bank and Co-operative Group IT separation programmes. This includes all data held by each of the parties’ group members, which for the Co-operative Group includes CFSMS and CIS General Insurance Limited;

(ii) To establish an appropriate data protection and security framework for the disclosure of data that is shared in order to facilitate the completion of the separation programmes; and

(iii) To provide an appropriate data protection and security framework for all other data sharing that is taking place between the Co-operative Group and the Bank, and their group members, in relation to which no written agreement containing adequate data protection provisions currently exists.

As part of the separation process, the Bank and members of the Co-operative Group had been negotiating to replace the IT Services Agreement and the 2006 Agreement with appropriate revised arrangements under a replacement agreement. However, such revisions are no longer being renegotiated as a result of the IT Separation Costs Agreement being entered into. Similarly, it is no longer proposed that the Professional Services Master Services Agreement be updated.

9.3 ***Relationship Agreement***

The Bank entered into a relationship agreement with the Co-operative Group and CBG on 4 November 2013 (the "**Relationship Agreement**") to regulate the basis of their ongoing relationship. It includes appropriate measures regarding the degree of control that the Co-operative Group, CBG and their associates may exercise over the management of the Bank.

For the purposes of the Relationship Agreement, a "significant shareholder" is any person (or persons acting jointly by agreement whether formal or otherwise) who is entitled to exercise, or to control the exercise of, 20 per cent. of the rights to vote at a general meeting of the Bank (as at 30 April 2015, the Co-operative Banking Group held 20.16 per cent. of the Bank's ordinary share capital). The Relationship Agreement records that, pursuant to the Articles of Association, the Co-operative Group has the right to appoint and, once appointed, remove persons to the Board of the Bank. The Co-operative Group's current shareholding allows it to appoint one director; this position is currently vacant.

Under the Relationship Agreement, the Co-operative Group undertakes that it will conduct transactions with the Bank on arm's length terms and not seek to influence the day-to-day running of the Bank. Amendments to existing contracts and arrangements in place between the Co-operative Group and the Bank will require the approval of a majority of independent directors. The Relationship Agreement contains provisions on conflicts and related party transactions. The Relationship Agreement also imposed a five-year lock-up restriction on a disposal of Ordinary Shares by the Co-operative Group. However, pursuant to an amendment made under the Variation Director Appointment Deed, this lock-up restriction ceased to have effect on 30 September 2014.

The Co-operative Group also undertakes that neither it, nor any member of its group, shall without the prior written consent of the Bank: (i) operate, establish or acquire any undertaking which constitutes a competing business for a period of the later of the third anniversary of the Liability Management Exercise becoming unconditional and three years from the date of termination of the Relationship Agreement (although the Co-operative Group is permitted to carry on business activities carried on at the date when the Liability Management Exercise became unconditional), or (ii) solicit for employment any of the directors (or their respective direct reports) or senior managers of the Bank for the same time period as applies in (i) above. The Relationship Agreement will terminate immediately (but without prejudice to accrued rights and obligations) if the Co-operative Group ceases to be a significant shareholder of the Bank. For a period of two years after termination of the Relationship Agreement or seven years after the Liability Management Exercise became unconditional, whichever is the later, the Co-operative Group has agreed to: (i) use the Bank as exclusive financial services provider in respect of clearing and certain other services (excluding lending) that are currently provided by the Bank to the Co-operative Group on an exclusive basis; (ii) use the Bank as principal financial services provider in respect of certain services (excluding lending) that have been provided by Bank to the Co-operative Group at any time during the 12-month period prior to the date of the Relationship Agreement to the extent the Bank has the capacity to provide such services; (iii) promote the Bank's banking business and facilitate and encourage the Co-operative Group's customers and members to hold bank accounts with, and otherwise use the services of, the Bank; and (iv) support (which, for the avoidance of doubt, shall not include any obligation on the Co-operative Group to make any financial contribution to the Bank in this regard) the enhancement and rejuvenation of the Co-op brand and franchise.

Provisions are included in the Relationship Agreement concerning the fact that the Co-operative Group and the Bank share many of the same customers and it is, therefore, necessary to mitigate risks and deal with practical issues concerning the processing of data.

9.4 ***Variation and Director Appointment Deed***

A variation and director appointment deed was entered into on 9 May 2014 between the Bank, the Co-operative Group and CBG (the "**Variation and Director Appointment Deed**"), which made certain amendments to the Relationship Agreement, including amending the Co-operative Group's power to appoint persons to the Board of the Bank in certain circumstances as set out in "*Directors, Senior Management and Corporate Governance—Corporate Governance—Nominee*

Directors". In addition, the Variation and Director Appointment Deed provided that the five year lock-up restriction on the Co-operative Group disposing of its Ordinary Shares ceased to apply with effect from 30 September 2014.

9.5 ***Shareholder Rights Agreement***

On 9 May 2014, the Bank entered into a shareholder rights agreement with SP Coop Investment, Ltd. (Cayman), Perry Capital UK LLP, Invesco Asset Management Limited and York Capital Management Europe (UK) Advisers LLP and the Co-operative Group (the "**Shareholder Rights Agreement**") which granted rights in addition to those contained in the Relationship Agreement. The Shareholder Rights Agreement grants rights to certain shareholders to nominate Directors to the Board of the Bank as set out in "*Directors, Senior Management and Corporate Governance—Corporate Governance—Nominee Directors*". On 23 April 2015, Charles Bralver was nominated under the terms of the Shareholder Rights Agreement by an affiliate of Silver Point to join the Board of the Bank as a Non-Executive Director. In addition, under the Shareholder Rights Agreement, the Co-operative Group will in certain circumstances have the right alongside certain other significant shareholders to require the Bank to assist in the launch of a secondary offering of ordinary shares, provided the exercising shareholders have committed to sell ordinary shares valued at not less than £100 million.

9.6 ***The Agreed Co-existence Principles***

The Bank and the Co-operative Group have agreed co-existence principles (the "**Agreed Co-existence Principles**"), to be expressed in an agreement on terms later agreed between the parties which is currently being negotiated (the "**Co-existence Agreement**"). The Agreed Co-existence Principles govern the use of trademarks containing "Co-operative" or "Co-op" and other associated trademarks owned by both parties.

The Agreed Co-existence Principles are as follows:

(a) Until a trigger event occurs, namely if the Bank removes or alters any of the provisions in its articles of association that entrench co-operative values and ethics without the Co-operative Group consent, the Co-operative Group cannot conduct any business under a brand that combines the words "Co-operative" or "Co-op" and "Bank".

(b) After the Relationship Agreement ends (with a minimum lock up of five years) but before a trigger event, the Bank is free to continue using the terms "Co-operative" and "Co-op" provided it does so in a way that does not confuse the public into believing that the Bank is still a part of the Co-operative Group. Where trademarks are required by the Bank for this, the Co-operative Group will grant a nonexclusive royalty free licence until a trigger event occurs.

(c) After the expiry of the Non-Compete period (the minimum lock up of five years for the Relationship Agreement plus a further three years) the Co-operative Group is free to conduct any financial services business under any of its brands, subject to the restriction placed on its use of "Co-operative" or "Co-op" with "Bank" as provided for above.

(d) Until the thirteenth anniversary of the Effective Date (five years after the end of the Non- Compete period defined in the Relationship Agreement) the Co-operative Group will not conduct any such business which competes with the Bank under a main business brand including the words "Co-operative" or "Co-op" but may include such words in supporting marketing and advertising materials to make it clear that the business is part of the Co-operative Group.

(e) The Bank and the Co-operative Group each own various trademarks, some of which are predominantly used by the other party. There will be an exchange of trademark registrations to ensure that at the outset of the Co-existence Agreement the trademarks are owned by the correctly entitled and utilising entity.

The defined "banking" field of use for the purposes of the Agreed Co-existence Principles and the Co–existence Agreement must ensure that it is fair to both the Bank and the Co-operative Group given each of their current and anticipated activities.

9.7 ***IT Security Services Agreement***

Under the IT costs separation agreement, both the Co-operative Group and CFSMS undertake to support activities for the separation of the Bank's IT infrastructure from the wider Co-operative group's IT infrastructure, to enable the smooth transition to IBM. Further, the Co-operative Group and CFSMS undertake that any notice to terminate the existing IT services agreement (in the case of the Co-operative Group) and the CFSMS-Bank Framework Agreement (in the case of CFSMS) would not take effect prior to 31 December 2017 to give the Bank sufficient time to separate the Bank's IT infrastructure. The IT separation costs agreement also allocated the contributions to be made towards The Co-operative Group's own costs of keeping the wider Co-operative group's existing IT infrastructure stable and operable during and following the Bank's separation of its IT infrastructure; to this end CBG (as the parent of CFSMS) undertook to contribute a maximum of £95 million towards such Co-operative Group costs, with the Bank to make a contribution of up to £25 million, based on a formula in the event that the total cost of this Co-operative Group project falls between £76 million and £120 million.

9.8 ***Loss Sharing Deed***

As part of the negotiations relating to the separation of the Bank from the Co-operative Group, the Bank and the Co-operative Group entered into a loss sharing deed relating to the surrender of group relief between the entities in the Bank's tax group and entities in the Co-operative Group tax group. This deed sets out the basis of the agreement by the Co-operative Group to take proactive steps to allow it to maximise its claim for tax losses from the Bank for the accounting periods to 31 December 2012 and 2013. The deed also addresses the terms of the payment by the Co-operative Group to the Bank for those tax losses. The 2014 Annual Report, which include a group relief debtor of £126.8 million (2013: £126.6 million), have been prepared on a basis consistent with the deed. The Bank receives payment from the Co-operative Group when the Co-operative Group realises the benefit of the losses surrendered and at the corporation tax rate at which the benefit is realised.

9.9 ***Letter of Intent with Capita***

The Bank has entered into a non-binding letter of intent agreement dated 12 November 2014 with Capita Business Services Limited ("Capita") in relation to the proposed outsourcing of its mortgage processing services for all of its residential mortgage portfolios. As part of the proposed transaction, 100 per cent. of the shares in Western Mortgage Services Limited ("**WMS**"), a wholly owned subsidiary of the Bank, would be transferred to Capita. WMS would then acquire the Bank's other mortgage processing and administration operations together and certain existing Bank staff servicing the mortgage portfolios would be transferred to WMS.

9.10 ***Deed of surrender and release***

On 1 January 2008 the Bank was granted a licence by the Co-operative Group to install and operate ATMs at a number of Co-operative Food stores in the UK. On 14 April 2014, the Co-operative Group served notice on the Bank to terminate this licence with effect from 1 January 2016. As part of a new arrangement between the Co-operative Group and another third party, on 20 November 2014 the Co-operative Group and the Bank entered into a deed for the Bank to surrender immediately any rights of occupation it may have in relation to these premises. In consideration for this early surrender, the Co-operative Group paid to the Bank £2.9 million, with a further £5.2 million to be received in 2015. The Bank entered into a simultaneous agreement with Cardtronics UK Limited for the sale of these ATMs in the Co-operative Group premises.

9.11 ***CFSMS-Bank Framework***

On 16 February 2006, the Bank and CFSMS entered into the CFSMS-Bank Services Agreement pursuant to which CFSMS provides assets such as office equipment, materials and office space, other facilities and services, and consultants who act as secondees to the Bank. The Bank provides CFSMS with an indemnity for all liabilities, losses, damages, costs and expenses of any nature as a result of CFSMS entering into and performing the agreement in respect of the assets, services and personnel provided to the Bank.

The Bank and CFSMS commenced unwinding this arrangement during 2014 with the transfer of the employment of most staff to the Bank, the transfer of assets to the Bank and the Bank entering in to numerous contracts with third party suppliers to replace those previously provided through CFSMS or the wider Co-operative group. These activities continue into 2015, in particular in respect of the Bank's transition of enterprise services to IBM.

9.12 ***IBM Outsourcing Agreement***

On 23 January 2015, the Bank announced it had entered into a contract with IBM to migrate its enterprise IT infrastructure from the Co-operative Group into IBM managed data centres and receive a full suite of managed services, enabling:

- Improved IT infrastructure and resilience;
- Significant progress in separating IT from the Co-operative Group; and
- The foundation for the further development of the Bank's digital offering.

The Bank will pay IBM £93 million to lead and implement the transition of these services to IBM data centres. The Bank has also entered into a 10 year managed service contract at a total cost of £275 million and has options to terminate throughout the life of the contract. The contract has productivity savings embedded within it that are expected to deliver a cumulative total of approximately £40 million of savings in later years compared to current run costs.

10. LOSS FORECAST

The risk factor entitled "*High operating costs, credit impairment, higher than expected conduct provisions and one off costs have significantly impacted the Bank's profitability. The Bank expects to be loss making at least through 2015 and 2016*" contains the following statement:

- "*…The Bank expects to be loss making at least through 2015 and 2016…*"

The Bank's 2014 annual report contains the following statements:

- "*…we expect to continue to be loss making for at least two years…*"; and
- "*…the Bank expects to be loss making for at least the next two years…*"

The statements above regarding profitability represent a profit forecast under the Prospectus Directive Regulation (EC/809/2004), as amended. The Directors have considered the above statements and continue to believe that they are valid based on the assumptions below.

Basis of preparation and principal assumptions

The principal assumptions on which the profit forecast is based comprise:

- Assumptions about factors that are within management's control including:
    - Project costs to be incurred in 2015 and 2016 in connection with the IT remediation, separation from the Co-operative Group and investment in a digital platform;
    - Negative fair value adjustments to be made from the merger of the Bank with the Britannia Building Society;
    - There will be an expected loss on asset sales as a result of the deleveraging of the Non-core Business;
    - The Bank's Core Business non-interest income will decline in 2015 and stabilise in 2016; and

    - There will be a large decline in the Bank's Non-core Business total income in 2015 which will turn negative in 2016.

- Assumptions about factors that are not within management's control including:

    - There will be no material change in legislation or regulatory capital and liquidity requirements impacting the Bank's operations;

    - There will be no material change in the accounting standards applicable to the Bank;

    - There will not be any material change in interest rates affecting the Bank from those currently applicable to the Bank;

    - There will not be any material improvement or deterioration in the economic and general trading environment currently prevailing in the UK; and

    - There will be no material change to the competitive environment which impacts on consumer preferences.

The profit forecast has been properly compiled on the basis of the stated assumptions and using accounting policies which are in accordance with IFRS and consistent with those used by the Bank in the year ended 31 December 2014 and which will be applicable for the financial years ending 31 December 2015 and 2016.

DIRECTORS, SENIOR MANAGEMENT AND CORPORATE GOVERNANCE

1. DIRECTORS

The following table lists the names and positions with respect to current Directors and the Company Secretary.

Name	Position
Dennis Holt	Chairman
Niall Scott Kilgour Booker	Chief Executive Officer
John Baines	Finance Director
John Richard Coates	Interim Senior Independent Director
Laura Carstensen	Non-Executive Director
Richard Graeme Barclay Hardie	Non-Executive Director
Maureen Laurie	Non-Executive Director
William Gennydd Thomas	Non-Executive Director
Derek Weir	Non-Executive Director
Charles Bralver	Non-Executive Director
Brona McKeown	Company Secretary

Dennis Holt – Chairman

Dennis joined the Board in February 2014 and, with effect from 27 October 2014, was appointed as the Chairman. Dennis's experience in banking and insurance spans 36 years as an executive and a further seven as a non-executive director, involving a wide range of economic and competitive environments. He spent 31 years at Lloyds TSB, latterly as main board executive director in charge of the retail bank. This was followed by 5 years at AXA Sun Life Services plc as UK chief executive and a member of the global executive committee. As a non-executive, he has served amongst others as chair of Liverpool Victoria and of Bank of Ireland plc , as well as deputy chair of Bank of Ireland UK. He is currently chairman of Beazley plc and its subsidiary Beazley Furlonge Limited.

Niall Scott Kilgour Booker – Chief Executive Officer

Niall joined the Board in June 2013. He has held a variety of senior roles at HSBC in a career of more than 30 years spanning retail and corporate banking. Most recently, he was group managing director and chief executive officer of HSBC North America Holdings Inc. In this role he had responsibility for working through the issues in HSBC Finance Corporation, where he was chief executive officer, including working closely with the regulators of HSBC North America Holdings. Niall has been a member of the committee of the council of Glenalmond College since 2012 and its chairman since 2013.

John Baines – Finance Director

John joined the Board in October 2014 but has been providing his services as Chief Financial Officer to the Bank since April 2013. He was most recently chief financial officer of Aldermore Bank plc, having spent the previous eight years at the Royal Bank of Scotland plc where he was initially chief financial officer of the wealth management division, being appointed as chief executive officer of the division in 2006. John is a qualified chartered accountant and, prior to the Royal Bank of Scotland plc, held a number of senior finance roles in investment banks, including spending six years at each of UBS and J.P. Morgan.

John Richard Coates – Interim Senior Independent Director

Richard joined the Board in January 2013. He has over 25 years' experience in the retail financial services sector. Richard was a senior partner at KPMG from 1985 to 2003 in its retail financial services practice. He joined Northern Rock plc as a non-executive director in August 2008 and chaired its audit committee from January 2010 until its acquisition by Virgin Money plc in January 2012. He is currently a non-executive director of the Police Mutual Assurance Society.

Richard Graeme Barclay Hardie – Non-Executive Director

Graeme joined the Board in May 2013. He was previously managing director of NatWest retail bank and executive director, retail banking at Abbey National Bank plc. He was a senior adviser in retail markets at the Financial Services Authority (as it was known) and non-executive director at Metro Bank (UK) Limited. He is currently a non-executive director of FNZ (UK) Ltd and is a director of Northpoint Consultancy Services Limited.

William Gennydd Thomas – Non-Executive Director

William joined the Board in October 2013. He is a former senior vice president of Hewlett-Packard and was on the executive committee of EDS plc as executive-vice president. He has IT expertise and is an experienced leader and general manager with a track record in leading major change in large organisations. He has extensive commercial and operational experience, working domestically and internationally with both public and private sector organisations. William is chair of the advisory board at Cranfield University School of Management and is on the management and board of Leeds University Business School. He is currently a non-executive director of Xchanging plc and GFI SA and a partner in Hopton Estates.

Laura Carstensen – Non-Executive Director

Laura Carstensen was appointed to the Board in May 2014. Laura is a former partner at the City firm, Slaughter and May. Laura is co-founder of two online mail order businesses, Blue Banyan Limited and Hortica Enterprises Limited is a senior advisor, National Audit Office, a member and deputy chair of The Competition & Markets Authority (formerly the Competition Commission) and a trustee, National Museums Liverpool. She is currently a non-executive director and chair of the audit committee of Park Group PLC, a non-executive director of MLEX Limited and a partner in Bryn Yorkin Manor Estate LLP.

Maureen Laurie – Non-Executive Director

Maureen joined the Board in June 2014. She brings over 30 years of experience in senior human resources (HR) roles spanning global HR strategy, policy and transformation for organisations such as the British Council, NYSE EURONEXT, LIFFE, Barclays Bank plc, Standard Chartered Bank, EBRD and Reuters. Maureen is currently a non-executive director and trustee of Reuters Pension Fund, a non-executive director, governor and trustee of London Metropolitan University.

Derek Weir – Non-Executive Director

Derek joined the Board in July 2014. He has over 25 years of financial services experience, holding a range of senior positions in corporate and commercial banking. During this time he held posts, both in the UK and internationally, at Barclays Bank plc and the Royal Bank of Scotland plc, including being the managing director responsible for commercial banking in the UK for the Royal Bank of Scotland plc. Derek is currently a non-executive director of Motherwell Football and Athletic Club Limited, Motherwell Football Club Community Trust and a director of Kerrach Limited.

Charles Bralver – Non-Executive Director

Charles joined the Board with effect from 23 April 2015. He was nominated under the terms of the Shareholder Rights Agreement by Silver Point, a shareholder in the Bank. Charles is a Senior Advisor on the global financial services sector to Silver Point and for the purposes of the UK Corporate Governance Code he will not be independent. Charles was a founding partner of Oliver Wyman & Company where from 1984 through to 2007, he held several positions, including Vice Chairman, Head of Europe, Head of North America, and Head of the Global Capital Markets Practice, and remains a member of Oliver Wyman's Senior Advisory Board. Charles is currently a board director for Canaccord Genuity and Newstar Financial. He has over 30 years' financial services experience, including two years as a Strategic Advisor on Financial Services at Warburg Pincus LLC. He is the former Senior Associate Dean for International Business and Finance at the Fletcher School of Law and Diplomacy at Tufts University in Boston, USA.

The business address of each of the Directors is c/o Secretariat, 4th Floor, Miller Street Tower, Miller Street, Manchester, England M60 0AL, United Kingdom.

2. SENIOR MANAGEMENT

In addition to the Chief Executive Officer and Finance Director, the current members of the senior executive management team with responsibility for day-to-day management of the Bank's business are:

Chris Page – Chief Risk Officer ("CRO")

Chris joined the Bank on 1 October 2014. He is an established CRO with extensive financial services experience, having worked for ANZ Limited and multiple roles at HSBC throughout Europe, Asia, north and south America, in both wholesale and retail banking. Chris brings a wealth of experience in risk, mortgages, credit and specialised lending. In 2011 he received the 'Asian Banker 2011 award for outstanding achievement in Risk Management'. Upon retiring from ANZ Limited and before joining the Bank, Chris established his own contractor small business company in Melbourne (Earnest Knight and Company Pty Limited) and Hong Kong (Earnest Knight and Company Limited).

Grahame McGirr – Managing Director, CoAM

Grahame was appointed as the Managing Director of CoAM on 1 May 2014. He previously provided his services as Chief Risk Officer to the Bank from 1 February 2013, and in addition had responsibility for CoAM from July 2013, under a services contract. Grahame has 17 years' experience in the industry. Prior to joining CBG Ltd, Grahame had a career with Barclays Bank plc, where he was head of portfolio trading, and Investec plc. Following the financial crisis, Grahame was part of the team that restructured Northern Rock Limited, followed by a period at the Royal Bank of Scotland plc.

Liam Coleman – Director, Retail and Commercial Bank

Liam was appointed as Director of the Retail and Commercial Bank on 1 September 2014. Liam joined the Bank in June 2013 as Treasurer. Liam has 25 years' experience in the industry and prior to joining the Bank, Liam was deputy group treasurer and group head of capital management at the Royal Bank of Scotland plc from February 2011 to June 2013 and he worked at Nationwide Building Society from 1996 to 2011, ultimately as group director, treasury where he had responsibility for all of the treasury activities of the society. Earlier in his career, Liam worked at NatWest Limited in corporate banking and at Hambros Limited and The Bank of Tokyo-Mitsubishi UFJ, Ltd. in corporate and structured finance. Liam is currently a non-executive director of Great Western Hospitals NHS Foundation Trust.

Julie Harding – HR Director

Julie was appointed as the HR Director on 1 May 2014 and has responsibility for developing and implementing a "People Strategy" that will restore the engagement, and stability of the Bank's employee base, reduce the overall cost base, address capability gaps and produce a credible and robust succession plan. This is underpinned by a culture change programme to support improvements in governance, risk management and the successful deployment of the business strategy. Julie has in excess of 30 years' experience in HR, primarily in the retail financial services sector. She has worked as a HR director in emerging and developed markets, domestically and internationally, within distressed and successful businesses and within "business as usual" and transformational programmes. Prior to joining the Bank, Julie led the Global HR transformation programme at HSBC Bank plc.

Steve Friedlos – Chief Information Officer ("CIO")

Steve joined the Bank in October 2014 taking overall responsibility for IT strategy and the delivery of all IT services needed to run the Bank. His first priority is to drive a technology transformation programme to separate the Bank from its former parent, the Co-operative Group.

Steve has held senior IT roles at various financial services firms, including investment banks, brokering, asset management and insurance. Prior to joining the Bank, Steve was the CIO for a European private banking group in Luxembourg.

Brona McKeown – General Counsel and Company Secretary

Brona joined the Bank as General Counsel and Company Secretary in December 2013. She has more than 20 years' experience advising on legal matters in financial services.

Brona trained and qualified in the City law firm, CMS Cameron McKenna LLP, before joining Barclays' Bank plc in-house legal team in 1998. She held a variety of roles at Barclays, culminating in being global general counsel of Barclays Corporate, a division of Barclays Bank plc. Brona left Barclays Bank plc in 2011. Before joining the Bank, Brona was interim general counsel and company secretary at the Coventry Building Society.

Steve Britain – Director of Strategy and Chief of Staff (interim)

Steve has been providing his services as Director of Strategy and Chief of Staff since November 2014 under a contract for the provision of services. He previously provided his services as Commercial Director and then as Director of Retail and Commercial Bank between November 2013 and October 2014. He has nearly 25 years' experience in the UK financial services.

Steve joined Midland Bank plc in 1990 as a graduate from Cambridge University and worked for HSBC Bank plc in UK retail banking and wealth management for more than 20 years. Most recently, he led the UK savings and investments business, the UK cards business and strategic transformation programmes in wealth management.

Chris Greenway –Director of Audit

Chris has been the Director of Internal Audit at the Bank since January 2015, with an 'Acting Director' role for the previous six months following the departure of David Rutherford, Interim Audit Director. Chris has 20 years' internal audit experience in financial services. Before joining the Bank, Chris held a variety of permanent leadership roles in Internal Audit, where he was Head of Audit. Prior to that Chris spent four years in a variety of leadership roles in the Barclays Bank plc Internal Audit team, including oversight of the legal & regulatory compliance, Barclaycard and UK retail bank audit teams. Before this Chris worked for Bank of America Merrill Lynch International Limited, Ernst & Young LLP and Aviva Limited.

Richard Wilson – Chief Administration Officer

Richard was appointed as the Chief Administration Officer on 5 May 2015, joining from TORI Ltd where he was engaged by the Bank to develop the target operating model. Richard has 25 years' industry experience. Prior to joining the Bank, Richard spent 10 years with Newedge Group SA as Chief Information Officer, Chief Operating Officer and ultimately the CEO of Newedge UK Financial Ltd. Previously, Richard spent 15 years with Société Générale in a variety of management roles in finance, operations and technology. Richard is currently non-executive chairman of Société Générale Newedge Ltd.

3. DIRECTORS' CONFLICT OF INTEREST

Save as set out below in this paragraph 3, none of the Directors has any potential conflict of interest between their duties to the Bank and their private interests and/or their duties to third parties. The Board recognises that, by virtue of being statutory directors as well as individuals who receive remuneration (in the form of directors' fees for Non-Executive Directors and salary, bonus, pensions or long term incentive plans for Executive Directors) from the Bank, they have an inherent personal interest in the financial performance, capital management and overall health of the financial status of the Bank.

The directors hold the interests set out below:

Dennis Holt

Chair	Beazley plc
Chair	Beazley Furlonge Limited
Shareholder	Lloyds Bank plc
Shareholder	Bank of Ireland
Pension	Lloyds Pension Scheme No.1 Limited

Niall Booker

Description	*Interest Held In*
Chair	Committee of Council of Glenalmond College Enterprises Limited. Shareholder of HSBC Holdings plc (relevant where HSBC has offered mandates, etc).
Pensioner of (currently deferred)	HSBC International Staff Retirements Benefit Scheme

John Baines

Description	*Interest Held In*
Director	JBC Liquidation Number 1 Limited
Pensioner of (currently deferred)	The Royal Bank of Scotland Group plc Pension Scheme

Richard Coates

Description	*Interest Held In*
Director	Police Mutual Assurance Society
Deferred pension scheme	KPMG Pension Scheme
Membership	

Richard Graeme Barclay Hardie

Description	*Interest Held In*
Director	Northpoint Consultancy Services Limited
Director	FNZ (UK) Limited
Pension	The Royal Bank of Scotland Group plc
Shareholder	The Royal Bank of Scotland Group plc
Shareholder	Santander UK plc
Shareholder	Metro Bank plc

William Gwynedd Thomas

Description	*Interest Held In*
LLP Member	The Invicta Film Partnership, LLP
Director	Xchanging plc
Director	LogicNow Holding S.à r.l
Chair of Advisory Board	Cranfield University School of Management
Member of Advisory Board	Leeds University Business School
Adviser	Adviser to the Labour Party on a variety of subjects including defence, business and skills policy
Partner	Hopton Estates Limited
Pension	Hewlett-Packard Limited
Connected Person (daughter)	Daughter employed by Cap Gemini S.A., which may be a supplier to Bank.

Laura Carstensen

Description	*Interest Held In*
Non Executive Director	Park Group plc
Director	MLEX Limited
Commissioner	Equality and Human Rights Commission
Trustee	National Museums Liverpool
Partner	Bryn Yorkin Manor Estate LLP
Owner	Blue Banyan Trading Limited
	Quatrefoil Ventures Limited

Maureen Laurie

Description	*Interest Held In*
Director	London Metropolitan University
Director	Reuters Pension Fund Limited
Pension (occupational)	Standard Chartered Bank Pension Fund Limited
Pension (deferred)	Reuters Pension Fund Limited

Derek Weir

Description	*Interest Held In*
Director	Motherwell Football And Athletic Club Limited (The)
Director	Motherwell Football Club Community Trust (company limited by guarantee)
Director	Kerrach Limited
Pension	The Royal Bank of Scotland Group plc
Pension	Barclays plc
Shareholder	The Royal Bank of Scotland Group plc

Charles Bralver

Description	*Interest Held In*
Non Executive Director	Newstar Financial Inc.
Non Executive Director	Canaccord Genuity Inc.
Senior Advisor	Oliver Wyman
Senior Advisor	Silver Point Capital LP

4. CORPORATE GOVERNANCE

The UK Corporate Governance Code, published by the Financial Reporting Council in September 2012 (the "**UK Corporate Governance Code"**), sets out standards of good practice in relation to board leadership and effectiveness, remuneration, accountability and relations with shareholders. The UK Corporate Governance Code recommends that at least half the board of directors (excluding the Chairman) should comprise "independent" non-executive directors. The UK Corporate Governance Code states that the board should determine whether a director is independent in character and judgement and whether there are any relationships or circumstances which are likely to affect, or could appear to affect, the director's judgement.

The Directors support high standards of corporate governance. As at the date of this Prospectus, the Bank complies with the principles of the UK Corporate Governance Code with the exception of B.61 being an external evaluation of the Board, A4.2 in relation to an appraisal of the Chairman's performance and C3.2 being the membership of risk committee, including a non-independent non-executive director. The Bank's Board of Directors currently comprises two Executive Directors (the Chief Executive Officer and the Finance Director) and eight Non-Executive Directors (including the Chairman). The Bank regards John Richard Coates, Laura Carstensen, Richard Graeme Barclay Hardie, Dennis Holt, Maureen Laurie, William Gennydd Thomas and Derek Weir as independent Non-Executive Directors, within the meaning of "independent" as defined in the UK Corporate Governance Code. The Bank appointed Dennis Holt as the Chairman with effect from 27 October 2014 and John Richard Coates as Interim Senior Independent Director in October 2014.

There remain three vacant Board positions where candidates are able to be nominated by shareholders for consideration by the nominations committee and the Board of the Bank.

Nominee Directors

As referred to in the relationship agreement entered into on 4 November 2013 by the Bank, the Co-operative Group and CBG, (the "**Relationship Agreement**"), for so long as it remains a bona fide co-operative society, the Articles of Association of the Bank provide Co-operative Group with the right to appoint and, once appointed, remove (i) up to two persons to the Board provided that Co-operative Group controls directly or indirectly 25 per cent. or more of the voting rights

exercisable at a general meeting of the Bank; or (ii) one person to the Board provided that Co-operative Group controls directly or indirectly 20 per cent. or more, but less than 25 per cent., of the voting rights exercisable at a general meeting of the Bank.

Under the terms of the variation and director appointment deed between the Bank, the Co-operative Group and CBG dated 11 May 2014, even if the Co-operative Group ceases to exercise, or to control, directly or indirectly, the exercise of 20 per cent. or more of the rights to vote at general meetings of the Bank (and therefore loses its right to have a director nominated under the Relationship Agreement) but remains a bona fide co-operative society and directly or indirectly controls 15 per cent. or more of the voting rights exercisable at general meetings of the Bank, it has the right to appoint one director to the Board. This position is currently vacant.

Subject to certain conditions, the Relationship Agreement also provides a mechanism for the appointment of up to two persons as non-executive directors (in each case, after having been identified for such purpose by the Purchasers) by the purchasers of additional ordinary shares during the Liability Management Exercise. On 25 July 2014, the Bank announced that under the terms of the Relationship Agreement, Derek Weir was nominated to be on the Board of the Bank as a Non-Executive Director. The second position is currently vacant.

The Shareholder Rights Agreement also grants rights in addition to those contained in the Relationship Agreement. Two of the Bank's largest shareholders are SP Coop Investment, Ltd. (Cayman) ("**Silver Point**") and Perry Capital UK LLP ("**Perry Capital**"). Under the Shareholder Rights Agreement, the Bank has granted to each of Silver Point and Perry Capital the right to nominate a director for appointment to the Board for so long as Silver Point and Perry Capital, as the case may be, directly or indirectly controls 5 per cent. or more of the voting rights exercisable at general meetings of the Bank. Such rights are not transferable, save that they will automatically transfer and be exercisable by certain other significant shareholders if Silver Point or Perry Capital ceases to control such level of voting rights in the Bank, provided that such other shareholder itself directly or indirectly controls 5 per cent. or more of such voting rights. Any such directors so nominated may, but are not required to, satisfy the criteria to be independent pursuant to the UK Corporate Governance Code.

On 23 April 2015, Charles Bralver was nominated under the terms of the Shareholder Rights Agreement by an affiliate of Silver Point to join the Board of the Bank as a Non-Executive Director. Charles is not considered as independent within the meaning of "independent" as defined under the UK Corporate Governance Code. The second position under the Shareholder Rights Agreement is currently vacant.

TAXATION

UNITED KINGDOM TAXATION CONSIDERATIONS

The following is a summary of certain United Kingdom stamp duty and stamp duty reserve tax considerations and the United Kingdom withholding taxation treatment at the date hereof in relation to payments of principal and interest in respect of the Notes. Save where expressly stated to the contrary, it is based on current law and the practice of Her Majesty's Revenue & Customs ("HMRC"), which may be subject to change, sometimes with retrospective effect. The comments do not deal with other United Kingdom tax aspects of acquiring, holding or disposing of the Notes. The comments relate only to the position of persons who are absolute beneficial owners of the Notes. The following is a general guide and should be treated with appropriate caution. It is not intended as tax advice and it does not purport to describe all of the tax considerations that might be relevant to a prospective purchaser. Holders who are in any doubt as to their tax position should consult their professional advisers. Holders who may be liable to taxation in jurisdictions other than the United Kingdom in respect of their acquisition, holding or disposal of the Notes are particularly advised to consult their professional advisers as to whether they are so liable (and if so under the laws of which jurisdictions), since the following comments relate only to certain United Kingdom taxation aspects of payments in respect of the Notes. In particular, holders should be aware that they may be liable to taxation under the laws of other jurisdictions in relation to payments in respect of the Notes even if such payments may be made without withholding or deduction for or on account of taxation under the laws of the United Kingdom.

Also investors should note that the appointment by an investor in Notes, or any person through which an investor holds Notes, of a custodian, collection agent or similar person in relation to such Notes in any jurisdiction may have tax implications. Investors should consult their own tax advisers in relation to the tax consequences for them of any such appointment.

UK Withholding Tax

*The Taxation of Regulatory Capital Securities Regulations 2013 (the "**2013 Regulations**")*

Interest on the Notes may be paid without withholding or deduction for or on account of United Kingdom income tax if the Notes constitute "regulatory capital securities" for the purposes of the 2013 Regulations and there are no arrangements, the main purpose, or one of the main purposes, of which is to obtain a tax advantage as a result of the application of the 2013 Regulations in respect of the Notes.

The Notes will constitute a "regulatory capital security" for the purposes of the 2013 Regulations provided the Notes qualify, or have qualified, as a Tier 2 instrument under Article 63 of the Commission Regulation (EU) No. 575/2013 and form, or formed, a component of Tier 2 capital for the purposes of Commission Regulation (EU) No 575/2013.

Quoted Eurobond Exemption

The Notes will constitute "quoted Eurobonds" provided they are and continue to be listed on a recognised stock exchange. Whilst the Notes are and continue to be quoted Eurobonds, payments of interest on the Notes may be made without withholding or deduction for or on account of United Kingdom income tax.

Notes will be "listed on a recognised stock exchange" for this purpose if they are admitted to trading on an exchange designated as a recognised stock exchange by an order made by the Commissioners for HMRC and either they are included in the United Kingdom official list (within the meaning of Part 6 of the FSMA) or they are officially listed, in accordance with provisions corresponding to those generally applicable in European Economic Area states, in a country outside the United Kingdom in which there is a recognised stock exchange.

The London Stock Exchange is a recognised stock exchange, and accordingly the Notes will constitute quoted Eurobonds provided they are and continue to be included in the United Kingdom official list and admitted to trading on the regulated market of that exchange.

In all cases falling outside the exemptions described above, interest on the Notes may fall to be paid under deduction of United Kingdom income tax at the basic rate (currently 20%) subject to such relief as may be available following a direction from HMRC pursuant to the provisions of any applicable double

taxation treaty, or to any other exemption which may apply. However, this withholding will not apply if the relevant interest is paid on Notes with a maturity date of less than one year from the date of issue and which are not issued under arrangements the effect of which is to render such Notes part of a borrowing with a total term of a year or more.

Provision of Information

HMRC has powers to obtain information, including in relation to interest or payments treated as interest and payments derived from securities. This may include details of the beneficial owners of the Notes (or the persons for whom the Notes are held), details of the persons to whom payments derived from the Notes are or may be paid and information in connection with transactions relating to the Notes. Information obtained by HMRC may be provided to tax authorities in other countries.

Other considerations

Where interest has been paid under deduction of United Kingdom income tax, Holders who are not resident in the United Kingdom may be able to recover all or part of the tax deducted if there is an appropriate provision in any applicable double taxation treaty.

The references to "interest" above mean "interest" as understood in United Kingdom tax law. The statements in above do not take any account of any different definitions of "interest" or principal" which may prevail under any other law or which may be created by the terms and conditions of the Notes or any related documentation.

The above description of the United Kingdom withholding tax position assumes that there will be no substitution of the issuer and does not consider the tax consequences of any such substitution.

Stamp duty and stamp duty reserve tax

No United Kingdom stamp duty or stamp duty reserve tax is payable on the issue of the Notes. Provided that the Notes are "regulatory capital securities" for the purposes of the 2013 Regulations (see the paragraph entitled "*UK Withholding Tax - The Taxation of Regulatory Capital Securities Regulations 2013*" above) and there are no arrangements, the main purpose, or one of the main purposes, of which is to obtain a tax advantage as a result of the application of the 2013 Regulations in respect of the Notes, no United Kingdom stamp duty or stamp duty reserve tax will be payable on the transfer of the Notes.

OTHER TAX CONSIDERATIONS

EU Savings Tax Directive

Under EC Council Directive 2003/48/EC on the taxation of savings income (the "**Savings Directive**"), each Member State is required to provide to the tax authorities of another Member State details of payments of interest or other similar income paid by a person within its jurisdiction to, or collected by such a person for, an individual resident or certain limited types of entity established in that other Member State; however, for a transitional period, Austria may instead apply a withholding system in relation to such payments, deducting tax at rates rising over time to 35 per cent. The transitional period is to terminate at the end of the first full fiscal year following agreement by certain non-EU countries to the exchange of information relating to such payments.

A number of non-EU countries including Switzerland, and certain dependent or associated territories of certain Member States, have adopted similar measures (either provision of information or transitional withholding) in relation to payments made by a person within its jurisdiction to, or collected by such a person for, an individual resident or, certain limited types of entity established in a Member State (a withholding system in the case of Switzerland). In addition, the Member States have entered into provision of information or transitional withholding arrangements with certain of those dependent or associated territories in relation to payments made by a person in a Member State to, or collected by such a person for, an individual resident or certain limited types of entity established in one of those territories.

The Council of the European Union formally adopted a Council Directive amending the Savings Directive on 24 March 2014 (the "**Amending Directive**"). The Amending Directive broadens the scope of the requirements described above. The Amending Directive requires Member States to apply these

new requirements from 1 January 2017 and if they were to take effect the changes made under the Amending Directive would extend the scope of the Savings Directive to payments made to, or collected for, certain other entities and legal arrangements. They also broaden the definition of "interest payment" to cover income that is equivalent to interest.

However, the European Commission has proposed the repeal of the Savings Directive from 1 January 2017 in the case of Austria and from 1 January 2016 in the case of all other Member States (subject to ongoing requirements to fulfil administrative obligations such as the reporting and exchange of information relating to, and accounting for withholding taxes on, payments made before those dates). This is to prevent overlap between the Savings Directive and a new automatic exchange of information regime to be implemented under Council Directive 2011/16/EU on Administrative Co-operation in the field of Taxation (as amended by Council Directive 2014/107/EU). The proposal also provides that, if it proceeds, Member States will not be required to apply the new requirements of the Amending Directive.

Investors who are in any doubt as to their position should consult their professional advisers.

The proposed financial transactions tax ("FTT")

On 14 February 2013, the European Commission published a proposal (the "**Commission's proposal**") for a Directive for a common FTT in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the "**participating Member States**").

The Commission's proposal has very broad scope and could, if introduced, apply to certain dealings in the Notes (including secondary' market transactions) in certain circumstances.

Under the Commission's proposal, FTT could apply in certain circumstances to persons both within and outside of the participating Member States. Generally, it would apply to certain dealings in the Notes where at least one party is a financial institution, and at least one party is established in a participating Member State. A financial institution may be, or be deemed to be, "established" in a participating Member State in a broad range of circumstances, including (a) by transacting with a person established in a participating Member State or (b) where the financial instrument which is subject to the dealings is issued in a participating Member State.

Joint statements issued by participating Member States indicate an intention to implement the FTT by 1 January 2016.

However, the FTT proposal remains subject to negotiation between the participating Member States and the scope of any such tax is uncertain. Additional EU Member States may decide to participate.

Prospective holders of the Notes are advised to seek their own professional advice in relation to the FTT.

SUBSCRIPTION AND SALE

HSBC Bank plc and UBS Limited (the "**Joint Lead Managers**") have, in a subscription agreement dated 29 June 2015 (the "**Subscription Agreement**") and made between the Issuer and the Joint Lead Managers, upon the terms and subject to the conditions contained therein, jointly and severally agreed to subscribe for the Notes at their issue price of 100 per cent. of their principal amount less a combined underwriting and management fee. The Issuer has also agreed to reimburse the Joint Lead Managers for certain of their expenses incurred in connection with the issue of the Notes and to indemnify them against losses incurred by them in specified circumstances relating to their appointment as Joint Lead Managers in respect of the Notes. The Joint Lead Managers are entitled in certain circumstances to be released and discharged from their obligations under the Subscription Agreement prior to the closing of the issue of the Notes.

United Kingdom

Each Joint Lead Manager has further represented, warranted and undertaken that:

(a) it has only communicated or caused to be communicated and will only communicate or cause to be communicated an invitation or inducement to engage in investment activity (within the meaning of Section 21 of the FSMA) received by it in connection with the issue or sale of the Notes in circumstances in which Section 21(1) of the FSMA would not, if the Issuer were not an authorised person, apply to the Issuer; and

(b) it has complied and will comply with all applicable provisions of the FSMA with respect to anything done by it in relation to the Notes in, from or otherwise involving the United Kingdom.

United States of America

The Notes have not been and will not be registered under the Securities Act and may not be offered or sold within the United States or to, or for the account or benefit of, U.S. persons except in accordance with regulation S under the Securities Act or pursuant to any other exemption from the registration requirements of the Securities Act. Terms used in this paragraph have the meanings given to them by Regulation S.

The Notes are subject to U.S. tax law requirements and may not be offered, sold or delivered within the United States or its possessions or to a United States person, except in certain transactions permitted by U.S. Treasury regulations. Terms used in this paragraph have the meanings given to them by the United States Internal Revenue Code of 1986 and Treasury regulations thereunder.

Each Joint Lead Manager has represented, warranted and agreed that it has not offered or sold, and will not offer or sell, any Notes constituting part of its allotment within the United States except in accordance with Rule 903 of Regulation S under the Securities Act. Each Manager has also represented, warranted and agreed that it has offered and sold the Notes, and will offer and sell the Notes (i) as part of their distribution at any time and (ii) otherwise until 40 days after the later of the commencement of the offering and the Closing Date (as defined in the Subscription Agreement), only in accordance with Rule 903 of Regulation S under the Securities Act, and that it will have sent to each dealer to which it sells Notes during the distribution compliance period a confirmation or other notice setting forth the restrictions on offers and sales of the Notes within the United States or to, or for the account or benefit of, U.S. persons.

In addition, until 40 days after commencement of the offering, an offer or sale of Notes within the United States by any dealer (whether or not participating in the offering) may violate the registration requirements of the Securities Act.

General

No action has been taken by the Issuer or either of the Joint Lead Managers that would, or is intended to, permit a public offer of the Notes or possession or distribution of this Prospectus or any other offering or publicity material relating to the Notes in any country or jurisdiction where any such action for that purpose is required. Accordingly, each Joint Lead Manager has undertaken that it will not, directly or indirectly, offer or sell any Notes or have in its possession, distribute or publish any offering circular, prospectus, form of application, advertisement or other document or information in any country or

jurisdiction except under circumstances that will, to the best of its knowledge and belief, result in compliance with any applicable laws and regulations and all offers and sales of Notes by it will be made on the same terms.

Without prejudice to the generality of the foregoing, each Joint Lead Manager has agreed that it will obtain any consent, approval or permission which is, to the best of its knowledge and belief, required for the offer, purchase or sale by it of Notes under the laws and regulations in force in any jurisdiction to which it is subject or in which it makes such offers, purchases or sales and it will, to the best of its knowledge and belief, comply with all such laws and regulations.

None of the Issuer, the Joint Lead Managers or the Trustee represents that the Notes may at any time lawfully be sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, or assumes any responsibility for facilitating such sale.

GENERAL INFORMATION

Authorisation

1. The creation and issue of the Notes has been duly authorised by resolutions of the Board of Directors of the Issuer dated 13 May 2015, 28 May 2015 and 11 June 2015.

Legal and Arbitration Proceedings

2. Save as disclosed in this Prospectus under "*Description of the Bank – 8. Litigation and Arbitration"*, there are no governmental, legal or arbitration proceedings, (including any such proceedings which are pending or threatened, of which the Issuer is aware), which may have, or have had during the 12 months prior to the date of this Prospectus, a significant effect on the financial position or profitability of the Issuer and its subsidiaries.

Significant/Material Change

3. There has been no material adverse change in the prospects of the Issuer since 31 December 2014, the date to which the Issuer's last published audited financial statements were prepared.

4. There has been no significant change in the financial or trading position of the Issuer and its subsidiaries since 31 December 2014, the date to which the Issuer's last published financial statements were prepared.

Auditors

5. The financial statements of the Issuer for the year ended 31 December 2013 have been audited in accordance with generally accepted auditing standards, by KPMG Audit Plc and are qualified by an "emphasis of matter", on page 124 of the 2013 Annual Report.

   On 30 May 2014, Ernst & Young LLP formally replaced KPMG Audit Plc as the Issuer's auditor following shareholder approval at the Issuer's annual general meeting. The financial statements for the year ended 31 December 2014 have been audited in accordance with generally accepted auditing standards by Ernst & Young LLP of 1 More London Place, London SE1 2AF and are qualified by an "emphasis of matter", on pages 140 and 141 of the 2014 Annual Report.

   Both emphasis of matter referred to above relate to the Bank's and its group's ability to continue as a "Going Concern".

   KPMG Audit Plc and Ernst & Young LLP are members of the Institute of Chartered Accountants in England and Wales.

Documents on Display

6. Copies of the following documents may be inspected during normal business hours on any weekday (Saturdays, Sundays and public holidays excepted) at the registered office of the Issuer at P.O. Box 101, 1 Balloon Street, Manchester M60 4EP for 12 months from the date of this Prospectus:

   (a) the Memorandum and Articles of Association of the Issuer;

   (b) the audited consolidated financial statements of the Issuer for the years ended 31 December 2014 and 2013;

   (c) the Trust Deed and Agency Agreement; and

   (d) this Prospectus.

Material Contracts

7. Save as disclosed under "*Description of the Bank—Material Contracts*", there are no material contracts entered into other than in the ordinary course of the Issuer's business which could result

in any member of the Issuer's group being under an obligation or entitlement that is material to the Issuer's ability to meet its obligations to Noteholders in respect of the Notes being issued.

Third Party Information

8. Where information in this Prospectus has been sourced from third parties, this information has been accurately reproduced and as far as the Issuer is aware and is able to ascertain from the information published by such third parties no facts have been omitted which would render the reproduced information inaccurate or misleading. The source of third party information is identified where it is used.

Clearing

9. The Notes have been accepted for clearance through Euroclear and Clearstream, Luxembourg. The ISIN is XS1249403541 and the common code is 124940354.

10. The address of Euroclear is Euroclear Bank SA/NV, 1 Boulevard du Roi Albert II, B-1210 Brussels and the address of Clearstream, Luxembourg is Clearstream Banking, 42 Avenue JF Kennedy, L-1855 Luxembourg.

Admission to trading

11. The total expenses related to the admission to trading of the Notes are estimated to be approximately £4,200.

THE ISSUER

The Co-operative Bank p.l.c.
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JOINT LEAD MANAGERS

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London EC2V 7EX

PRINCIPAL PAYING AGENT AND CALCULATION AGENT

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REGISTRAR

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AUDITORS TO THE ISSUER

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