

LBG CAPITAL NO. 2 PLC

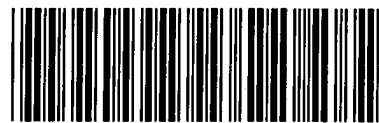
REPORT AND FINANCIAL STATEMENTS

FOR THE YEAR ENDED

31 DECEMBER 2015

Company Registration No: 07045669
Incorporated in England and Wales

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LBG CAPITAL NO. 2 PLC

REPORT AND FINANCIAL STATEMENTS

For the year ended 31 December 2015

Registered in England and Wales as a public limited company No.07045669

Registered office: 25 Gresham Street, London, United Kingdom EC2V 7HN.

DIRECTORS

V. D. Savadia

R.D. Shrimpton

A.T. Rougier

COMPANY SECRETARY

M.A.A. Johnson

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LBG CAPITAL NO. 2 PLC ("the Company")

STRATEGIC REPORT

For the year ended 31 December 2015

PRINCIPAL OBJECTIVES AND STRATEGIES

The Company was incorporated on 15 October 2009. The Company's principal activity is to hold investments and issue capital securities on behalf of Lloyds Banking Group plc ("LBG" or the "Group").

BUSINESS MODEL

The Company's assets consist of subordinated notes issued by Lloyds Bank plc and its liabilities are principally Enhanced Capital Notes ("ECN's") issued to market investors.

PERFORMANCE REVIEW

The profit after taxation for the year of £34,283,000 (2014: £535,562,000) is set out in the Statement of Comprehensive Income on page 8. No dividends were paid during 2015 (2014: £300,000,000).

Total assets as at 31 December 2015 were £2,569,666,000 (2014: 2,630,246,000) with net assets of £82,613,000 (2014: £48,330,000).

There were no changes in the nature of the Company's operations during the year and there are no changes expected in the foreseeable future.

During March 2014, LBG made an offer to Retail and Institutional investors which would enable the Group to strengthen its capital position in line with regulatory requirements. The Group offered eligible Retail investors who held outstanding Sterling denominated Enhanced Capital Notes the opportunity to exchange their ECNs for cash. The Group also offered Institutional investors the opportunity to exchange ECNs, into a new instrument called Additional Tier 1 securities ("AT1"). The AT1 securities were issued by the ultimate parent company.

Approximately £21m was exchanged by Retail investors for cash. In addition, approximately £1.25bn ECNs held by Institutional investors was exchanged for approximately £1.33bn AT1s. The exchange resulted in a loss of £41,660,966. The company also sold a similar amount of intercompany debt securities assets to Lloyds Banking Group plc for a premium and this resulted in gain on sale of £545,943,797.

PRINCIPAL RISKS AND UNCERTAINTIES

From the perspective of the Company, the principal risks and uncertainties are integrated with the principal risks of LBG and are not managed separately. Full disclosure of the Company's financial risk management objectives and policies are given in note 15 to the financial statements.

KEY PERFORMANCE INDICATORS ("KPIs")

Given the straightforward nature of the business, the Company's directors are of the opinion that analysis using key performance indicators is not necessary for an understanding of the development, performance or position of the business.

DIRECTORS' REPORT

The directors present their report and the audited financial statements of the Company for the year ended 31 December 2015.

DIRECTORS

The names of the directors of the Company, all of whom served throughout the year and up to the date of signing the financial statements are shown on page 1.

The following changes have taken place during the year:

V. D. Savadia (Appointed 29 February 2016)

E.F.G. Short (Resigned 31 January 2016)

During the year the previous company secretary (P. Gittins) resigned on 18 December 2015 and M.A.A. Johnson was appointed the company secretary on 18 December 2015.

DIRECTORS' REPORT (CONTINUED)

For the year ended 31 December 2015

STATEMENT OF DIRECTORS' RESPONSIBILITIES

The directors are responsible for preparing the strategic report, directors' report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have prepared the financial statements in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union ("the EU"). Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and accounting estimates that are reasonable and prudent;
- state whether applicable International Financial Reporting Standards (IFRSs) as adopted by the European Union, and IFRSs as issued by the International Accounting Standards Board (IASB), have been followed, subject to any material departures disclosed and explained in the financial statements;
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

DIRECTORS' INDEMNITIES

Lloyds Banking Group plc has granted to the Directors of the Company, a deed of indemnity through deed poll which constituted 'qualifying third party indemnity provisions' for the purposes of the Companies Act 2006. The deed was in force during the whole of the financial year and at the date of approval of the financial statements or from the date of appointment in respect of the director who joined the board of the Company during the financial year. Directors no longer in office but who served on the Board of the Company at any time in the financial year had the benefit of this contract of indemnity during that period of service. The indemnity remains in force for the duration of a Director's period of office. The deed indemnifies the Directors to the maximum extent permitted by law. The Deed for existing Directors is available for inspection at the registered office of Lloyds Banking Group plc. In addition, the Group has in place appropriate Directors and Officers Liability Insurance cover which was in place throughout the financial year.

GOING CONCERN

The Company is reliant on funding provided by the Group. The Directors are satisfied that it is the intention of Lloyds Banking Group plc that its subsidiaries including the Company will continue to have access to adequate liquidity and capital resources for the foreseeable future and, accordingly, the financial statements have been prepared on a going concern basis.

The Company is expected to be profitable in future accounting periods.

SUBSEQUENT EVENTS

Beside the subsequent event stated in note 9, there are no further events after the balance sheet that the directors are aware of that they require to bring to the attention of the users of the financial statements.

LBG CAPITAL NO. 2 PLC

DIRECTORS' REPORT (CONTINUED)

For the year ended 31 December 2015

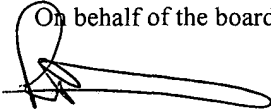
INDEPENDENT AUDITORS AND AUDIT INFORMATION

Each director in office at the date of this report confirms that, so far as the director is aware, there is no relevant audit information of which the Company's auditors are unaware and each director has taken all the steps that he or she ought to have taken as a director in order to make himself or herself aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

This confirmation is given, and should be interpreted, in accordance with the provisions of section 418 of the Companies Act 2006.

PricewaterhouseCoopers LLP are deemed to be re-appointed as auditors under section 487(2) of the Companies Act 2006.

On behalf of the board



R.D. Shrimpton

Director

Date: 24 May 2016

Company Registration No : 07045669

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF LBG CAPITAL NO. 2 PLC
Report on the financial statements

Our opinion

In our opinion, LBG Capital No.2 plc's financial statements (the "financial statements"):

- give a true and fair view of the state of the company's affairs as at 31 December 2015 and of its profit and cash flows for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards ("IFRSs") as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

What we have audited

The financial statements, included within the Report and Financial Statements (the "Annual Report"), comprise:

- the Balance Sheet as at 31 December 2015;
- the Statement of Comprehensive Income for the year then ended;
- the Cash Flow Statement for the year then ended;
- the Statement of Changes in Equity for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is IFRSs as adopted by the European Union, and applicable law.

In applying the financial reporting framework, the directors have made a number of subjective judgements, for example in respect of significant accounting estimates. In making such estimates, they have made assumptions and considered future events.

Opinion on other matter prescribed by the Companies Act 2006

In our opinion, the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

Under the Companies Act 2006 we are required to report to you if, in our opinion:

- we have not received all the information and explanations we require for our audit; or
- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns.

We have no exceptions to report arising from this responsibility.

Directors' remuneration

Under the Companies Act 2006 we are required to report to you if, in our opinion, certain disclosures of directors' remuneration specified by law are not made. We have no exceptions to report arising from this responsibility.

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 4, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland) ("ISAs (UK & Ireland)"). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

This report, including the opinions, has been prepared for and only for the parent company's members as a body in accordance with Chapter 3 of Part 16 of the Companies Act 2006 and for no other purpose. We do not, in giving these opinions, accept or assume responsibility for any other purpose or to any other person to whom this report is shown or into whose hands it may come save where expressly agreed by our prior consent in writing.

LBG CAPITAL NO. 2 PLC

For the year ended 31 December 2015

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF LBG CAPITAL NO. 2 PLC (CONTINUED)

What an audit of financial statements involves

We conducted our audit in accordance with ISAs (UK & Ireland). An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of:

- whether the accounting policies are appropriate to the company's circumstances and have been consistently applied and adequately disclosed;
- the reasonableness of significant accounting estimates made by the directors; and
- the overall presentation of the financial statements.

We primarily focus our work in these areas by assessing the directors' judgements against available evidence, forming our own judgements, and evaluating the disclosures in the financial statements.

We test and examine information, using sampling and other auditing techniques, to the extent we consider necessary to provide a reasonable basis for us to draw conclusions. We obtain audit evidence through testing the effectiveness of controls, substantive procedures or a combination of both.

In addition, we read all the financial and non-financial information in the Report and Financial Statements to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.



Stuart Scoular (Senior Statutory Auditor)
for and on behalf of PricewaterhouseCoopers LLP
Chartered Accountants and Statutory Auditors
London

24 May 2016

LEG CAPITAL NO. 2 PLC**STATEMENT OF COMPREHENSIVE INCOME**

For the year ended 31 December 2015

	Note	2015 £'000	2014 £'000
Interest and similar income		238,400	281,099
Interest and similar expense		<u>(201,460)</u>	<u>(258,914)</u>
Net interest income	3	36,940	22,185
Net trading income / (expense)	4	6,529	8,626
Other operating income	5	<u>-</u>	<u>504,283</u>
Profits before taxation		43,469	535,094
Taxation	7	<u>(9,186)</u>	<u>468</u>
Profit for the year		<u>34,283</u>	<u>535,562</u>
Total comprehensive income for the year		<u>34,283</u>	<u>535,562</u>

All activities are continuing. The Company has no gains and losses other than those included in the results above.

The accompanying notes on pages 12 to 26 form an integral part of the financial statements.

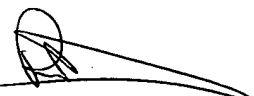
LBG CAPITAL NO. 2 PLC

BALANCE SHEET

As at 31 December 2015

	Note	2015 £000	2014 £000
ASSETS			
Current assets			
Cash and cash equivalents		294,590	303,797
Other current assets	8	114,396	117,670
Amounts owed by other group companies - debt securities held as loans and receivables	14	<u>2,160,680</u>	<u>-</u>
Total current assets		<u>2,569,666</u>	<u>421,467</u>
Non-current assets			
Amounts owed by other group companies - debt securities held as loans and receivables	14	<u>-</u>	<u>2,208,779</u>
Total non-current assets		<u>-</u>	<u>2,208,779</u>
Total assets		<u>2,569,666</u>	<u>2,630,246</u>
LIABILITIES			
Current liabilities			
Subordinated liabilities	9	2,363,012	-
Other current liabilities	11	114,576	117,399
Current tax liabilities	10	<u>9,249</u>	<u>10,383</u>
Total current liabilities		<u>2,486,837</u>	<u>127,782</u>
Non-current liabilities			
Subordinated liabilities	9	-	2,453,855
Deferred taxation	12	<u>216</u>	<u>279</u>
Total non-current liabilities		<u>216</u>	<u>2,454,134</u>
Total liabilities		<u>2,487,053</u>	<u>2,581,916</u>
EQUITY			
Share capital	13	50	50
Accumulated profit		<u>82,563</u>	<u>48,280</u>
Total equity		<u>82,613</u>	<u>48,330</u>
Total liabilities and equity		<u>2,569,666</u>	<u>2,630,246</u>

The financial statements were approved by the Board of Directors on 24 May 2016 and signed on its behalf by:



R.D. Shrimpton
Director

The accompanying notes on pages 12 to 26 form an integral part of the financial statements.

LBG CAPITAL NO. 2 PLC

STATEMENT OF CHANGES IN EQUITY

For the year ended 31 December 2015

	Share Capital	Accumulated (Losses)	Total
	£'000	/Retained Profits	Equity
	£'000	£'000	£'000
Balance at 31 December 2013	50	(187,282)	(187,232)
Profit and total comprehensive income for the year	-	535,562	535,562
Dividends paid	-	(300,000)	(300,000)
Balance at 31 December 2014	50	48,280	48,330
Profit and total comprehensive income for the year	-	34,283	34,283
Balance at 31 December 2015	50	82,563	82,613

The accompanying notes on pages 12 to 26 form an integral part of the financial statements.

LBG CAPITAL NO. 2 PLC

CASH FLOW STATEMENT

For the year ended 31 December 2015

	Note	2015 £'000	2014 £'000
Cash flows from operating activities			
Profit before taxation		43,469	535,094
<u>Adjustment for:</u>			
Interest income	3	(238,400)	(281,099)
Interest expense	3	201,460	258,914
Foreign exchange movement		(6,600)	(8,661)
Net gain on securities	5	-	(504,283)
Operating profit before working capital changes		(71)	(35)
Decrease in other current liabilities		-	(188)
Taxation paid		(10,383)	(65,212)
Net cash used in operating activities		(10,454)	(65,435)
Cash flows from investing activities			
Proceeds from disposal of debt securities		26,832	1,739,927
Advances to group companies	14	(18,858)	-
Interest received		239,119	340,705
Net cash provided by investing activities		247,093	2,080,632
Cash flows from financing activities			
Repayment of subordinated liabilities		-	(1,385,969)
Dividends paid		-	(300,000)
Interest paid		(245,846)	(346,983)
Net cash used in financing activities		(245,846)	(2,032,952)
Changes in cash and cash equivalents		(9,207)	(17,755)
Cash and cash equivalents at beginning of the year		303,797	321,552
Cash and cash equivalents at end of the year		294,590	303,797

The accompanying notes on pages 12 to 26 form an integral part of the financial statements.

NOTES TO THE FINANCIAL STATEMENTS

For the year ended 31 December 2015

1. ACCOUNTING POLICIES**1. BASIS OF PREPARATION**

The financial statements have been prepared under the historical cost convention, in compliance with the requirements of the Companies Act 2006 and in accordance with the applicable International Financial Reporting Standards ("IFRSs") as adopted by the European Union and interpretations issued by the IFRS-Interpretations Committee (IFRS-IC).

The Company is reliant on funding provided by the Group. The Directors are satisfied that it is the intention of Lloyds Banking Group plc that its subsidiaries including the Company will continue to have access to adequate liquidity and capital resources for the foreseeable future and, accordingly, the financial statements have been prepared on a going concern basis.

The principal accounting policies applied in the preparation of these financial statements are set out below. These policies have been applied consistently for each of the periods presented, unless otherwise stated.

The preparation of the financial statements necessarily requires the exercise of judgment both in the application of accounting policies which are set out in the sections below and in the selection of assumptions used in the calculation of estimates. These estimates and judgments are reviewed on an ongoing basis and are continually evaluated based on historical experience and other factors. Actual results may differ from these estimates.

The following pronouncements were effective during the year and relevant to the Company:

<u>Pronouncement</u>	<u>Nature of change</u>	<u>IASB effective date</u>
Annual improvements 2013 (endorsed for annual periods on or after 1 January 2015)	The amendments include changes from the 2011-2-13 cycle of the annual improvements project that affect 4 standards: <ul style="list-style-type: none">• IFRS 1, 'First time adoption'• IFRS 3, 'Business combinations'• IFRS 13, 'Fair value measurement' and• IAS 40, 'Investment property'.	Endorsed for annual periods on or after 1 January 2015

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

Annual improvements 2012	<p>These amendments include changes from the 2010-12 cycle of the annual improvements project, that affect 7 standards:</p> <ul style="list-style-type: none"> • IFRS 2, 'Share-based payment' • IFRS 3, 'Business Combinations' • IFRS 8, 'Operating segments' • IFRS 13, 'Fair value measurement' • IAS 16, 'Property, plant and equipment' and IAS 38, 'Intangible assets' • Consequential amendments to IFRS 9, 'Financial instruments', • IAS 37, 'Provisions, contingent liabilities and contingent assets', and • IAS 39, Financial instruments – Recognition and measurement'. 	Annual periods beginning on or after 1 July 2014
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The following pronouncements will be relevant to the Company but were not effective as at 31 December 2015:

<u>Pronouncement</u>	<u>Nature of change</u>	<u>IASB effective date</u>
Annual improvements 2014	<p>These set of amendments impacts 4 standards:</p> <ul style="list-style-type: none"> • IAS 19, 'Employee benefits' regarding discount rates. • IAS 34, 'Interim financial reporting' regarding disclosure of information. • IFRS 7, 'Financial instruments: Disclosures', (with consequential amendments to IFRS 1) regarding servicing contracts. • IFRS 5, 'Non-current assets held for sale and discontinued operations' regarding methods of disposal. <p>The company is currently assessing the impact of "Annual improvements 2014".</p>	Annual periods beginning on or after 1 January 2016
IFRS 9 'Financial instruments'	<p>This standard replaces the guidance in IAS 39. It includes requirements on the classification and measurement of financial assets and liabilities; it also includes an expected credit losses model that replaces the current incurred loss impairment model.</p> <p>The company is currently assessing the impact of IFRS 9 "Financial Instruments".</p>	Annual periods beginning on or after 1 January 2018
Amendment to IAS 1, 'Presentation of financial statements' on the disclosure initiative	<p>These amendments are as part of the IASB initiative to improve presentation and disclosure in financial reports. effective for annual periods beginning on or after 1 January 2016, subject to EU endorsement. In brief INT2014-18 looks at the details.</p> <p>The company is currently assessing the impact of "Amendment to IAS 1".</p>	Annual periods beginning on or after 1 January 2016

There are other pronouncements, new standards and amendments which were published in 2015 but are not relevant to the Company.

(a) Revenue recognition

Interest income and expense are recognised in the Statement of Comprehensive Income for all interest-bearing financial instruments, using the effective interest method. The effective interest method is a method of calculating the amortised cost

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

of a financial asset or liability and of allocating the interest income or interest expense. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts over the expected life of the instrument to the net carrying amount of the financial asset or financial liability. The calculation includes all amounts paid or received by the Company that are an integral part of the overall return, direct incremental transaction costs related to the acquisition, issue or disposal of a financial instrument and all other premiums or discounts. Fees and commissions, which are not an integral part of the effective interest rate, are generally recognised when the service has been provided.

(b) Income taxes, including deferred income taxes

Current income tax which is payable on taxable profits is recognised as an expense in the year in which the profits arise. Deferred tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the Company's financial statements. Deferred tax is determined using tax rates that have been enacted or announced by the balance sheet date that are expected to apply when the related deferred tax asset is realised or the deferred tax liability is settled. Deferred tax assets are recognised where it is probable that future taxable profit will be available against which the temporary differences can be utilised.

(c) Cash and cash equivalents

Cash and cash equivalents comprises cash on hand and demand deposits as well as short-term, highly liquid investments that are readily convertible to known amounts of cash and which are subject to an insignificant risk of changes in value.

(d) Loans and receivables

Loans and receivables are accounted for at amortised cost using the effective interest method. Loans and receivables are initially recognised when cash is advanced to the borrowers at fair value inclusive of transaction costs.

(e) Available-for-sale financial assets

Investments in designated common interests where the Company does not control the operating activities or financial and operating policies of the investee are classified as available-for-sale and recognised in the balance sheet at their fair value. Gains and losses arising from changes in the fair value of investments classified as available-for-sale including any foreign exchange component are recognised directly in equity, until the financial asset is either sold, becomes impaired or matures, at which time the cumulative gain or loss previously recognised in equity is recognised in the statement of comprehensive income.

(f) Debt securities held as loans and receivables

Debt securities for which there is no active market are classified as loans and receivables. They are initially recognised at fair value plus directly related transaction costs and are subsequently carried on the balance sheet at amortised cost using the effective interest method less provision for impairment.

(g) Impairment

At each balance sheet date the Company assesses whether, as a result of one or more events occurring after initial recognition, there is objective evidence that a financial asset has become impaired. If there is objective evidence that an impairment loss has been incurred, a provision is established which is calculated as the difference between the balance sheet carrying value of the asset and the present value of estimated future cash flows discounted at that asset's original effective interest rate.

(h) Derecognition of financial assets and liabilities

Financial assets are derecognised when the contractual right to receive cash flows from those assets has expired or when the Group has transferred its contractual right to receive the cash flows from the assets and either: substantially all of the risks and rewards of ownership have been transferred; or the Group has neither retained nor transferred substantially all of the risks and rewards, but has transferred control.

Financial liabilities are derecognised when they are extinguished (i.e. when the obligation is discharged), cancelled or expire.

(i) Borrowings

Borrowings (which include amounts from group companies, debt securities in issue and subordinated liabilities) are recognised initially at fair value, being their issue proceeds net of transaction costs incurred. These instruments are subsequently measured at amortised cost using the effective interest method. The coupons paid on these instruments are recognised in the statement of comprehensive income as interest expense.

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

(j) Foreign currency translation

Foreign currency transactions are translated into sterling using the exchange rates prevailing at the dates of the transactions. Foreign exchange gains and losses resulting from the settlement of such transactions and from the translation at year-end exchange rates of monetary assets and liabilities denominated in foreign currencies are recognised in the statement of comprehensive income.

(k) Dividend receivable and payable

Dividends on ordinary and preference shares treated as equity are recognised in equity in the year in which they are paid. Dividends in respect of investment in ordinary shares are recognised as income in the year in which they are received.

(l) Segment reporting

The chief operating decision maker is the board of directors. The board of directors manages the business as a single operating segment.

(m) Contingent liabilities

Contingent liabilities are possible obligations whose existence depends on the outcome of uncertain future events or those present obligations where the outflows of resources are uncertain or cannot be measured reliably. Contingent liabilities are not recognised in the financial statements but are disclosed unless they are remote.

2. CRITICAL ACCOUNTING JUDGEMENTS

The Company makes assumptions and estimates that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgments are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

The accounting policies deemed critical to the Company's results and financial position, based upon materiality and significant judgments and estimates, are discussed below.

Impairment

The Company determines that financial assets are impaired when there has been a significant or prolonged decline in the fair value below its cost. This determination of what is significant or prolonged requires judgment. In making this judgment, the Company evaluates when there is evidence of deterioration in the counterparties ability to pay the contractual cash flows.

3. NET INTEREST INCOME

	2015 £'000	2014 £'000
<i>Interest Income</i>		
Amount owed by other group companies - debt securities held	237,207	279,479
Cash balance with other group companies	<u>1,193</u>	<u>1,620</u>
	238,400	281,099
<i>Interest Expense</i>		
Subordinated liabilities	<u>201,460</u>	<u>258,914</u>
	201,460	258,914
Net interest income	<u><u>36,940</u></u>	<u><u>22,185</u></u>

4. NET TRADING INCOME

	2015 £'000	2014 £'000
Foreign exchange differences	<u>6,529</u>	<u>8,626</u>
	<u><u>6,529</u></u>	<u><u>8,626</u></u>

5. OTHER OPERATING INCOME

	2015 £'000	2014 £'000
Net gain on securities	<u>-</u>	<u>504,283</u>
	<u><u>-</u></u>	<u><u>504,283</u></u>

In March 2014, LBG made an offer to Retail and Institutional investors to buy back Enhanced Capital Notes (ECNs) which

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

would enable the Group to strengthen its capital position in line with regulatory requirements. The transaction resulted in gain on sale of internally held debt securities of £545,943,797 and a loss of £41,660,966 in relation to exchange of ECNs.

6. ADMINISTRATION EXPENSE

	2015 £'000	2014 £'000
Statutory audit fee	-	-

The number of persons employed by the Company during the year was nil (2014: nil). Statutory audit fees for the current year of £15,000 (2014: £15,000) were borne by Lloyds Bank plc.

7. TAXATION
(a) Analysis of tax (charge)/credit for the year

	2015 £'000	2014 £'000
UK Corporation tax - current year	(9,132)	691
UK Corporation tax - prior year adjustment	(117)	(466)
Deferred taxation (Note 12)	63	243
Total taxation for the year	(9,186)	468

The tax (charge)/credit on the company's profit for the year is based on a UK corporation tax rate 20.25% (2014: 21.5%).

(b) Factors affecting the tax (charge)/credit for the year

A reconciliation of the tax (charge)/credit that would result from applying the standard UK corporation tax rate to profit before tax to the tax (charge)/credit for the year is given below:

	2015 £'000	2014 £'000
Profits before taxation	43,469	535,094
Tax charge UK corporation tax rate of 20.25% (2014: 21.5%)	(8,802)	(115,045)
Deferred tax rate change	11	(18)
Adjustment in respect of prior years	(117)	(466)
Disallowed and non-taxable items	(278)	115,997
Total taxation (charge)/credit	(9,186)	468
Effective rate	21.13 %	(0.09%)

The Finance Act 2013 which was substantively enacted on 2 July 2013 reduced the main rate of corporation tax to 21% with effect from 1 April 2014 and 20% with effect from 1 April 2015.

The Finance (No. 2) Act 2015 which was substantively enacted on 26 October 2015 reduced the main rate of corporation tax to 19% with effect from 1 April 2017 and 18% with effect from 1 April 2020.

On 16 March 2016, the Government announced that the corporation tax rate applicable from 1 April 2020 would be 17%. The proposed reductions in the rate of corporation tax are expected to be enacted, and the impact accounted for, during 2016.

8. OTHER CURRENT ASSETS

	2015 £'000	2014 £'000
Interest receivable from other group companies - debt securities	114,396	117,670
	114,396	117,670

LBG CAPITAL NO. 2 PLC

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

9. SUBORDINATED LIABILITIES

(a)	2015 £'000	2014 £'000
Enhanced Capital Notes (refer to b below)	2,383,203	2,478,624
Capitalised issuance costs (refer to c below)	<u>(20,191)</u>	<u>(24,769)</u>
	<u><u>2,363,012</u></u>	<u><u>2,453,855</u></u>

(b)	ECN 2015 £'000	ECN 2014 £'000
Enhanced Capital Notes:		
At beginning of the year	2,478,624	3,933,333
Repayments during the year	-	(1,344,307)
Net accretion of (discounts)/premium	(48,204)	(26,541)
Foreign exchange movement	<u>(47,218)</u>	<u>(83,861)</u>
	<u><u>2,383,202</u></u>	<u><u>2,478,624</u></u>

Accrued Interest	<u>114,520</u>	<u>117,344</u>
At end of the year (refer to d below)	<u><u>2,497,722</u></u>	<u><u>2,595,968</u></u>

(c)	2015 £'000	2014 £'000
Capitalised issuance costs:		
At beginning of the year	(24,769)	(46,256)
Amortised during the year	<u>4,578</u>	<u>21,487</u>
At end of the year	<u><u>(20,191)</u></u>	<u><u>(24,769)</u></u>

(d) Details of the Enhanced Capital Notes are provided in the table below:

Rates	Product Name	Series	Notional at 31/12/15 (million)	2015 Carrying Value £'000	2014 Carrying Value £'000
8.875%	Enhanced Capital Notes due 2020	12	€125	101,643	108,242
9.334%	Enhanced Capital Notes due 2020	14	£21	22,743	22,834
6.385%	Enhanced Capital Notes due 2020	18	€614	439,842	460,640
15%	Enhanced Capital Notes due 2019	21	£704	904,824	936,368
15%	Enhanced Capital Notes due 2019	22	€487	466,497	513,285
15%	Enhanced Capital Notes due 2029	23	£68	105,099	106,404
9.125%	Enhanced Capital Notes due 2020	27	£46	49,005	49,133
11.125%	Enhanced Capital Notes due 2020	31	£4	4,520	4,581
12.75%	Enhanced Capital Notes due 2020	34	£13	15,791	16,131
7.625%	Enhanced Capital Notes due 2019	39	£40	38,760	38,479
9%	Enhanced Capital Notes due 2019	40	£15	15,857	15,892
14.5%	Enhanced Capital Notes due 2022	42	£15	19,894	20,402
9.875%	Enhanced Capital Notes due 2023	44	£5	5,828	5,854
11.25%	Enhanced Capital Notes due 2023	45	£19	22,127	22,366
10.5%	Enhanced Capital Notes due 2023	46	£9	9,675	9,742
11.875%	Enhanced Capital Notes due 2024	47	£16	19,570	19,799
9%	Enhanced Capital Notes due 2029	49	£1	646	646
8.5%	Enhanced Capital Notes due 2032	50	£3	3,506	3,503
16.125%	Enhanced Capital Notes due 2024	52	£14	20,972	21,442
7.875%	Enhanced Capital Notes due 2020		\$329	<u>230,923</u>	<u>220,225</u>
				<u><u>2,497,722</u></u> *	<u><u>2,595,968</u></u>

* Includes carrying value of £4,941,000 which were held by Lloyds Bank plc.

During March 2014, Lloyds Banking Group plc made an offer to Retail and Institutional investors to buy back Enhanced Capital Notes (ECNs) to enable the Group to strengthen its capital position. From the offers accepted, ECNs held by retail investors were exchanged for cash while those held by Institutional investors were exchanged into a new instrument called

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

9. SUBORDINATED LIABILITIES (CONTINUED)

Additional Tier 1 securities ("AT1"). The AT1 securities were issued by the ultimate parent company.

The ECNs contain an equity conversion feature that requires them to convert into ordinary shares if the consolidated core tier 1 ratio of Lloyds Banking Group plc falls below 5 per cent (based on a fixed definition as defined by the Financial Services Authority in May 2009). The conversion feature meets the definition of an embedded derivative and has been recorded separately as a derivative asset in the ultimate parent company and consolidated financial statements of Lloyds Banking Group plc. The conversion feature reflects the value to Lloyds Banking Group plc from the equity conversion feature contained within the ECNs. Only the liability component is held by the Company.

The ECNs issued by the Company are guaranteed by Lloyds Bank. Lloyds Bank has irrevocably and unconditionally guaranteed the due and punctual payment of all principal, premium and interest and any other sums, from time to time, expressed to be payable by the Company in respect of the ECNs and the related coupons and under Trust Deeds dated 1 December 2009 in respect thereof. The obligations under the guarantee constitute direct and unsecured obligations of Lloyds Bank subordinated as described in the conditions of the ECNs set out in the Trust Deeds dated 1 December 2009.

In the event that Lloyds Banking Group plc published consolidated Core Tier 1 ratio falls below 5% the Company shall pay to the ECN holders any accrued unpaid interest in respect of the ECNs and shall redeem the ECNs at a price equal to their principal amount. ECN holders shall be deemed irrevocably to have directed and authorised the Company to pay the principal amount to Lloyds Banking Group plc as consideration for Lloyds Banking Group plc agreement to issue ordinary shares and the obligations of the Company to pay principal on the relevant ECNs to holders shall be discharged by the Company's obligation to pay the principal amount to Lloyds Banking Group plc.

Following a relevant change of law event or certain disqualifying event, the Company may elect to redeem the ECNs for their principal amount together with accrued but unpaid interest (or such other amount specified in the relevant contractual terms).

The ECNs will, in the event of the winding-up of the Company, be subordinated to the claims of depositors and all other creditors of Lloyds Banking Group plc, other than creditors whose claims rank equally with, or are junior to, the claims of the holders of the subordinated liabilities. The subordination of specific subordinated liabilities is determined in respect of the Company and any guarantors of that liability. The claims of holders of preferred shares and securities are generally junior to those of the holders of undated subordinated liabilities, which in turn are junior to the claims of holders of the dated subordinated liabilities. The subordination of the ECNs ranks equally with that of the dated subordinated liabilities. No repayment or purchase by the issuer of the subordinated liabilities may be made prior to their stated maturity without the consent of the Financial Services Authority.

In 2015, the Group participated in the UK-wide concurrent stress testing run by the Bank of England; the Enhanced Capital Notes (ECNs) in issue were not taken into account for the purposes of core capital in the PRA stress tests and the Group has determined that a Capital Disqualification Event (CDE), as defined in the conditions of the ECNs, has occurred.

On 31 March 2015, the Lloyds Banking Group plc announced that it had received permission from the Prudential Regulation Authority (PRA) for the redemption of certain series of ECNs. It also confirmed that the Group had been notified by the Trustee that it would seek declaratory judgement in respect of the interpretation of certain terms of the ECNs. A judgement was handed down on 3 June 2015 and it concluded that despite the ECNs not being taken into account for the most recent stress test applied by the PRA, the ECNs may still be taken into account for future stress tests. As a result of the judgement, the Group has sought permission to appeal to the Court of Appeal.

The CDE determination was confirmed by a unanimous decision by the Court of Appeal on 10 December 2015 and on 29 January 2016 the Group announced the redemption of certain series of ECNs using the Regulatory Call Right. The Group also launched tender offers for the remaining series of ECNs on 29 January 2016. The Group redeemed those ECNs not validly tendered using the Regulatory Call Right. The result of the tender and Regulatory Call of the ECNs was a loss to the Company of £183m which included the write off of the premium and capitalised issuance costs. In addition, debt securities originally issued by Lloyds Bank plc (the "Debt Securities") were re-purchased resulting in a profit for the Company of 723m. As a result of this post balance sheet event the ECNs and the Debt Securities were reclassified from non-current liabilities to current liabilities and from non-current asset to current assets respectively.

The trustee of the ECNs has been granted leave by the Supreme Court to appeal the Court of Appeal decision. In the event that the Supreme Court were to determine that a CDE had not occurred, the Company would compensate fairly the holders of the ECNs whose securities are redeemed using the Regulatory Call Right for losses suffered as a result of early redemption.

LBG CAPITAL NO. 2 PLC

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

10. CURRENT TAX LIABILITIES

	2015	2014
	£'000	£'000
Corporation tax payable	<u>9,249</u>	<u>10,383</u>
	<u>9,249</u>	<u>10,383</u>

11. OTHER CURRENT LIABILITIES

	2015	2014
	£'000	£'000
Interest payable on enhanced capital notes	114,520	117,344
Interest payable to other group companies	<u>56</u>	<u>55</u>
	<u>114,576</u>	<u>117,399</u>

12. DEFERRED TAXATION

	2015	2014
	£'000	£'000
At beginning of the year	279	522
Deferred tax rate change	(11)	18
Deferred tax adjustment in respect of current year	<u>(52)</u>	<u>(261)</u>
At end of the year	<u>216</u>	<u>279</u>

The Finance Act 2013 which was substantively enacted on 2 July 2013 reduced the main rate of corporation tax to 21% with effect from 1 April 2014 and 20% with effect from 1 April 2015.

The Finance (No. 2) Act 2015 which was substantively enacted on 26 October 2015 reduced the main rate of corporation tax to 19% with effect from 1 April 2017 and 18% with effect from 1 April 2020.

On 16 March 2016, the Government announced that the corporation tax rate applicable from 1 April 2020 would be 17%. The proposed reductions in the rate of corporation tax are expected to be enacted, and the impact accounted for, during 2016.

13. SHARE CAPITAL

	2015	2014	2015	2014
	Number of shares	Number of shares	£	£
Issued and fully paid:				
At the beginning of the year	<u>50,000</u>	<u>50,000</u>	<u>50,000</u>	<u>50,000</u>
At the end of the year	<u>50,000</u>	<u>50,000</u>	<u>50,000</u>	<u>50,000</u>

The holder is entitled to 100% of the voting rights.

There is no contractual requirement to make dividend payments on the A ordinary share; hence they are classified as equity in line with IAS 32.

No interim dividends were paid during 2015. During 2014, an interim dividend of £6,000 pounds per ordinary share amounting to £300 million was proposed and paid to the parent company. No final dividend was proposed by the directors in respect of the year ending 31 December 2015 (2014: nil).

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

14. RELATED PARTY TRANSACTIONS

The Company's immediate parent company is LBG Capital Holdings Ltd which is wholly owned by Lloyds Banking Group plc. The Company regarded by the directors as the ultimate parent company and controlling party is Lloyds Banking Group plc, which is the parent undertaking of the largest group of undertakings for which group financial statements are drawn up and of which the Company is a member. Copies of the group financial statements may be obtained from the Company Secretary's office, Lloyds Banking Group plc, 25 Gresham Street, London EC2V 7HN. The Company's related parties include its ultimate parent company, fellow subsidiaries and pension schemes of the Company's ultimate parent company and the Company's key management personnel. Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company, which is determined to be the Company's directors.

Transactions with key management personnel

There were no transactions between the Company or its subsidiaries with key management personnel during the current year. Key management personnel and directors are employed by other companies in the Lloyds Banking Group plc and consider that their services to the Company are incidental to their other activities with the Group. Directors emoluments for the year is therefore nil (2014: nil).

Other transactions with other group companies

	2015	2014
	£'000	£'000
Lloyds Bank plc – Cash at Bank	294,590	303,797
Interest received (note 3)	<u>(1,193)</u>	<u>(1,620)</u>

Amounts owed by other group companies- debt securities held as loans and receivables

	2015	2014
	£'000	£'000
At beginning of the year	2,208,779	3,452,432
Advances during the year	18,858	-
Repayments during the year	(26,832)	(1,193,983)
Foreign exchange movement	<u>(40,125)</u>	<u>(49,670)</u>
	<u>2,160,680</u>	<u>2,208,779</u>
Representing:		
Lloyds Bank plc	<u>2,160,680</u>	<u>2,208,779</u>
	<u>2,160,680</u>	<u>2,208,779</u>
Interest Income earned (note 3)	237,207	279,479
Interest Income receivable (note 8)	<u>114,396</u>	<u>117,670</u>

The debt securities held are initially recorded at fair value at acquisition and are subsequently measured at amortised cost.

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT

The Company uses financial instruments to meet the financial needs of its counterparties and to reduce its own exposure to fluctuations in interest rates. The Company makes loans to other Lloyds Banking Group plc. companies at fixed rates and for various years.

(a) Interest Rate Risk

Interest rate risk arises from the mismatch between interest rate sensitive liabilities and interest rate sensitive assets. From the perspective of the Company, the interest rate risks are integrated with the interest rate risks of the group and are not managed separately. The scenarios are run only for assets and liabilities that represent the major interest-bearing positions. Based on the simulations performed, the full year impact on post-tax profit of a 0.25% shift would be an increase or decrease of approximately £183,940 (2014: £115,239).

The table below summarises the repricing mismatches of the Company's non-trading assets and liabilities. Items are allocated to time bands by reference to the earlier of the next contractual interest rate repricing date and the maturity date. Expected repricing and maturity dates do not differ significantly from the contract dates.

As at 31 December 2015	1 month or less £'000	3 months or less but over 1 month £'000	1 year or less but over 3 months £'000	5 years or less but over 1 year £'000	Over 5 years £'000	Non- interest bearing £'000	Total £'000
<i>Assets:</i>							
Amounts owed by group companies - debt securities held as loans and receivables	-	2,160,680	-	-	-	-	2,160,680
Cash and cash equivalents	294,590	-	-	-	-	-	294,590
Other current assets	-	-	-	-	-	114,396	114,396
Total financial assets	294,590	2,160,680	-	-	-	114,396	2,569,666
<i>Liabilities:</i>							
Subordinated liabilities	-	2,363,012	-	-	-	-	2,363,012
Other current liabilities	-	-	-	-	-	114,576	114,576
Current tax liabilities	-	-	-	-	-	9,249	9,249
Total financial liabilities	-	2,363,012	-	-	-	123,825	2,486,837
Total interest sensitivity gap	294,590	(202,332)	-	-	-	(9,429)	82,829

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

As at 31 December 2014	1 month or less £'000	3 months or less but over 1 month £'000	1 year or less but over 3 months £'000	5 years or less but over 1 year £'000	Over 5 years £'000	Non- interest bearing £'000	Total £'000
<i>Assets:</i>							
Amounts owed by other group companies - debt securities held as loans and receivables	-	-	-	1,309,818	898,961	-	2,208,779
Cash and cash equivalents	303,797	-	-	-	-	-	303,797
Other current assets	-	-	-	-	-	117,670	117,670
Total financial assets	303,797	-	-	1,309,818	898,961	117,670	2,630,246
<i>Liabilities:</i>							
Subordinated liabilities	-	-	-	1,418,426	1,035,429	-	2,453,855
Other current liabilities	-	-	-	-	-	117,399	117,399
Current tax liabilities	-	-	-	-	-	10,383	10,383
Total financial liabilities	-	-	-	1,418,426	1,035,429	127,782	2,581,637
Total interest sensitivity gap	303,797	-	-	(108,608)	(136,468)	(10,112)	48,609

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

(b) Foreign Exchange Risk

The Company is exposed to currency risk (or foreign exchange risk) through its subordinated liabilities and its loans and deposits to group companies. The Company's policy is to match its exposure to foreign currencies with equivalent currency-denominated loans from, or deposits with, its fellow subsidiary company, Lloyds-Bank-plc. Some residual currency exposure arises from slight mismatches in the funding held and from timing differences in arranging funding. The Company's level of exposure to currency risk is monitored according to the LBG's policies.

The Company's principal net exposures are to the Euro and US Dollar.

The Company's foreign currency exposure as at 31 December 2015 is as follows:

Gross Exposures	2015	2014
	£'000	£'000
EUR	(109,387)	(176,668)
USD	(22,083)	(38,733)

If Sterling had been weaker against the Euro or US Dollar by 10% at 31 December 2015 (10% at 31 December 2014) the impact would be a loss of £10,939,000 for the EUR exposure and a loss of £2,208,000 for the USD exposure (31 Dec 2014; £17,667,000 loss for the EUR exposure and £3,873,000 loss for the USD exposure).

The following significant exchange rates applied during the year:

	Average rate		Reporting date spot rate	
	2015	2014	2015	2014
EUR to GBP	1.3824	1.2393	1.3600	1.2826
USD to GBP	1.5258	1.6514	1.4814	1.5585

(c) Fair Value of Financial Assets and Liabilities

Financial instruments include financial assets and financial liabilities. The fair value of a financial instrument is the amount at which the instrument could be exchanged in a current transaction between willing parties, other than in a forced or liquidation sale.

Wherever possible, fair values have been estimated using quoted market prices for instruments held or the most recent price at which the transaction occurred. Where market prices are not available, fair values have been estimated using quoted values for instruments with either identical or similar characteristics. In certain cases, where no ready markets currently exist, various techniques (such as discounted cash flows or observations of similar recent market transactions) have been developed to estimate what the approximate fair value of such instruments might be. These estimation techniques are necessarily subjective in nature and involve several assumptions.

The Company provides loans and advances to other LBG companies at fixed and floating rates. The fair value for these loans and advances as disclosed in note 15 were estimated by discounting anticipated cash flows at a rate which reflects the effects of interest rate changes, adjusted for changes in credit risk. The fair values are at a specific date and may be significantly different from the amounts which will actually be paid or received on the maturity or settlement date.

Debt securities held by the Company are initially recorded at fair value and subsequently as loans and receivables at amortised cost.

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

Valuation hierarchy

The table below analyses the fair values of the financial assets and liabilities of the Group which are carried at amortised cost. They are categorised into levels 1 to 3 based on the degree to which their fair value is observable.

	Carrying value		Fair value	
	2015	2014	Level 2	Level 2
	2015	2014	2015	2014
	£'000	£'000	£'000	£'000
Financial assets				
Amount owed by other group companies - debt securities held as loans and receivables	2,160,680	2,208,779	2,990,904	3,288,029
Financial liabilities				
Subordinated liabilities	2,363,012	2,453,855	2,697,075	2,695,021

(d) Measurement Basis of Financial Assets and Liabilities

The accounting policies in note 1 describe how different classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following table analyses the carrying amounts of the financial assets and liabilities by category and by balance sheet heading.

As at 31 December 2015	Loans and receivables	Held at amortised cost	Total
	£'000	£'000	£'000
<i>Assets:</i>			
Amounts owed by other group companies - debt securities held	2,160,680	-	2,160,680
Cash and cash equivalents	-	294,590	294,590
Other current assets	-	114,396	114,396
Total financial assets	2,160,680	408,986	2,569,666

<i>Liabilities:</i>			
Subordinated liabilities	-	2,363,012	2,363,012
Other current liabilities	-	114,576	114,576
Total financial liabilities	-	2,477,588	2,477,588

As at 31 December 2014	Loans and receivables	Held at amortised cost	Total
	£'000	£'000	£'000
<i>Assets:</i>			
Amounts owed by other group company - loan balances	2,208,779	-	2,208,779
Cash and cash equivalents	-	303,797	303,797
Other current assets	-	117,670	117,670
Total financial assets	2,208,779	421,467	2,630,246

<i>Liabilities:</i>			
Subordinated liabilities	-	2,453,855	2,453,855
Other current liabilities	-	117,399	117,399
Total financial liabilities	-	2,571,254	2,571,254

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

(e) Credit Risk

The maximum credit risk exposure of the Company in the event of other parties failing to perform their obligations is detailed below. The maximum exposure to loss is considered to be the balance sheet carrying amount as at the year end.

	2015	2014
	£'000	£'000
Amounts owed by other group companies - debt securities held		
as loans and receivables	2,160,680	2,208,779
Cash and cash equivalent	294,590	303,797
Other current assets	114,396	117,670
Total credit risk exposure	<u>2,569,666</u>	<u>2,630,246</u>

The current rating of the ultimate parent company, Lloyds Banking Group plc, is Baa1, and the current rating of Lloyds Bank plc, is A1 as per Moody's. None of the assets is past due nor impaired.

(f) Liquidity Risk

The table below analyse liabilities of the Company on an undiscounted future cash flow basis according to contractual or actual maturity date into relevant maturity groupings based on the remaining period at the balance sheet date. Due to the post balance sheet event described in Note 9, the ECNs have been reclassified from non-current to current liabilities; therefore, the maturities of the subordinated liabilities have been disclosed in the 1-3 months time bucket. For 2014, the balances with no fixed maturity are included in the over 5 years category.

As at 31 December 2015	On demand	Up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Subordinated liabilities	-	-	2,324,320	-	-	-	2,324,320
Other current liabilities	55	75,474	16,551	22,494	-	-	114,574
Total Liabilities	<u>55</u>	<u>75,474</u>	<u>2,340,871</u>	<u>22,494</u>	<u>-</u>	<u>-</u>	<u>2,438,894</u>
As at 31 December 2014	On demand	up to 1 month	1 - 3 months	3 - 12 months	1 - 5 years	Over 5 years	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Subordinated liabilities	-	9,381	5,733	118,940	2,211,499	1,218,859	3,564,412
Other current liabilities	55	76,919	16,762	23,663	-	-	117,399
Total Liabilities	<u>55</u>	<u>86,300</u>	<u>22,495</u>	<u>142,603</u>	<u>2,211,499</u>	<u>1,218,859</u>	<u>3,681,811</u>

(g) Capital Risk Management

The Company's objectives when managing capital are to provide returns for shareholders and benefits for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital. In order to maintain or adjust the capital structure, the Company may adjust the amount of dividends paid to shareholders, return capital to shareholders, issue new shares or sell assets to reduce debt

Notes to the Financial Statements (continued)

For the year ended 31 December 2015

15. FINANCIAL RISK MANAGEMENT (CONTINUED)

The company monitors capital on the basis of the gearing ratio. This ratio is calculated as net debt (including 'current and non-current borrowings' as shown in the balance sheet) divided by total capital. Total capital is calculated as 'equity' as shown in the balance sheet plus net debt.

	As at 31/12/2015 £'000	As at 31/12/2014 £'000
Total liabilities	2,486,606	2,581,916
Less: cash and cash equivalents	<u>(294,590)</u>	<u>(303,797)</u>
Net debt	2,192,016	2,278,119
Total equity	<u>83,060</u>	<u>48,331</u>
Total capital	<u>2,275,076</u>	<u>2,326,450</u>
Gearing ratio	96 %	98 %

16. CONTINGENT LIABILITIES

The Group provides for potential tax liabilities that may arise on the basis of the amounts expected to be paid to tax authorities. This includes open matters where Her Majesty's Revenue and Customs (HMRC) adopt a different interpretation and application of tax law which might lead to additional tax. The Group has an open matter in relation to a claim for group relief of losses incurred in its former Irish banking subsidiary, which ceased trading on 31 December 2010. In 2013 HMRC informed the Group that their interpretation of the UK rules, permitting the offset of such losses, denies the claim; if HMRC's position is found to be correct management estimate that this would result in an increase in current tax liabilities for the company of approximately £76m (including interest). The Group does not agree with HMRC's position and, having taken appropriate advice, does not consider that this is a case where additional tax will ultimately fall due.

17. SUBSEQUENT EVENTS

Beside the subsequent event stated in note 9, there are no further events after the balance sheet that the directors are aware of that they require to bring to the attention of the users of the financial statements.