

COUTTS & CO

Directors' Report and Financial Statements

31 December 2006

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COUTTS & CO

REPORT AND FINANCIAL STATEMENTS 2006

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COUTTS & CO

OFFICERS AND PROFESSIONAL ADVISERS

DIRECTORS

The Earl of Home CVO, CBE (Chairman, Non-executive director)
Gordon Francis Pell (Non-executive director)
The Rt Hon Lord Hurd of Westwell CH, CBE (Deputy Chairman, Non-executive director)
Sir Frederick Anderson Goodwin (Non-executive director)
Sarah Jane Deaves (Chief Executive)
John Duncan Baines (Executive director)
Brian John Crowe (Non-executive director)
Nicholas Guy Pollard (Executive Director Appointed 15 February 2006)
Kathryn Anne Winup (Executive Director Appointed 15 February 2006)

SECRETARY

Sally Anne Doyle

REGISTERED OFFICE

440 Strand
London
WC2R 0QS

AUDIT COMMITTEE

The Earl of Home CVO, CBE (Chairman)
Neil Christopher Dolby
David Robert Edwards
William Stephen Pearson

AUDITORS

Deloitte & Touche LLP
London

Registered in England and Wales

DIRECTORS' REPORT

The directors present their annual report and the audited financial statements for the year ended 31 December 2006

ACTIVITIES AND BUSINESS REVIEW

Coutts & Co ('the Bank' or 'the Company') and its subsidiary undertakings (together called 'the Group') provide a wide range of banking and financial services

The Group continues to focus on its core activities of supplying wealth management and banking services to high net worth individuals and their businesses and will continue to concentrate on improving the quality and efficiency of the services provided

The Group is a member of The Royal Bank of Scotland Group plc which provides the Company with direction and access to all central resources it needs and determines policies in all key areas such as finance, risk, human resources or environment. For this reason, the directors believe that performance indicators specific to the Company are not necessary or appropriate for an understanding of the development, performance or position of the business. The annual reports of The Royal Bank of Scotland Group plc review these matters on a group basis. Copies can be obtained from Group Secretariat, RBS Gogarburn, Edinburgh, EH12 1HQ, the Registrar of Companies or through the Group's web site at rbs.com

The directors are satisfied with the development of the Company's activities during the year. The Company will be guided by its ultimate parent company in seeking further opportunities for growth. No final dividend has been declared (2005 - £Nil). No interim dividend has been paid (2005 - £12,500,000).

The Company's financial performance is presented in the Income Statement on Page 9. At the end of the year, the financial position showed total assets of £13,304,062,000 and equity of £428,639,000.

The Company is funded by facilities from The Royal Bank of Scotland plc and NatWest plc. It seeks to minimise its exposure to external financial risks other than credit risk, further information is disclosed in Note 27.

After making appropriate enquiries, the directors have satisfied themselves that the Group has adequate resources to continue in operational existence for the foreseeable future. For this reason, they continue to adopt the going concern basis in preparing the accounts.

Following a recent review of the Coutts & Co Investment Management Limited service the Board has decided that due to increasingly complex regulations it will no longer be able to undertake business for US resident clients. This business will be wound up during 2007 with precise timing still being determined.

The directors do not anticipate any other material change in either the type or level of business activities of the Company in the foreseeable future.

DIRECTORS AND SECRETARY

The present membership of the Board and secretary are set out on page 1. On 3 January 2006 Gordon Pell stood down as Chief Executive and was replaced by Sarah Deaves. Gordon Pell remains on the Board in a non-executive capacity. On 15 February 2006 Kathryn Winup and Nicholas Pollard were appointed as executive directors of the Company. All other directors served throughout the year.

DIRECTORS' REPORT
DISCLOSURE OF INFORMATION TO AUDITORS

Each of the directors at the date of approval of this report confirms that

- a) so far as he/she is aware there is no relevant audit information of which the Company's auditors are unaware, and
- b) the director has taken all the steps that he/she ought to have taken to make himself/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 shall be interpreted in accordance with the provisions of section 234ZA of the Companies Act 1985

DIRECTORS' INDEMNITIES

Under the terms of Section 309c of The Companies Act 1985 (as amended), all the Directors listed on page 1 have been granted Qualifying Third Party Indemnity Provisions by The Royal Bank of Scotland Group plc

DIRECTORS' INTERESTS

Shares

The interests of those who were directors at 31 December 2006 in the ordinary shares of the Royal Bank of Scotland Group plc ('RBS Group') were as follows

	Ordinary shares of £0.25 each	
	As at 1 January 2006 or date of appointment if later	As at 31 December 2006
S Deaves	2,935	13,519
J Baines	534	8,260
B Crowe	165,053	206,091
N Pollard	150	7,809
K Winup	211	1,935

Sir F Goodwin and Mr G Pell are directors of RBS Group and their interests in the ordinary shares and share options of RBS Group are disclosed in the 2006 Annual Report and Accounts of that company

The Earl of Home had a non-beneficial interest in 1840 RBS Group ordinary shares as at 1 January 2006 and nil RBS Group ordinary shares as at 31 December 2006

The other directors did not have any interests in RBS Group ordinary shares during the year

DIRECTORS' REPORT (continued)

Share options

Options to subscribe for ordinary shares of 25p each in RBS Group granted to and exercised by directors during the year to 31 December 2006 are included in the table below

	As at 1 January 2006 or date of appointment if later	Granted options	Price (£)	Exercised options	Price (£)	As at 31 December 2006
S Deaves	57,083	270 13,330	13 84 18 52	153 283	12 35 13 07	70,247
J Baines	42,182	17,549	18 52	-	-	59,731
B Crowe	199,845	40,780	18 52	40,500 150 150	12 37 15 63 12 40	199,825
N Pollard	-	186 8,774	13 84 18 52	-	-	8,960
K Winup	769	-	-	769	12 35	-

RBS Group options are exercisable at prices between 1,209p and 1,852p per share

No director had an interest in the Floating Rate Unsecured Loan Notes 2005 of The Royal Bank of Scotland Group plc during the year to 31 December 2006

No director had an interest in any of the preference shares of The Royal Bank of Scotland Group plc during the year to 31 December 2006

Other interests

According to the Register held by the Bank, none of the directors had any beneficial interests during the year in the shares of the Bank or of its subsidiary undertakings and no member of the immediate family of any director was granted or exercised any rights to subscribe for shares of the Bank or of its subsidiary undertakings

Sir F Goodwin, Mr G Pell and Mr B Crowe received no remuneration in relation to their position as directors of the Bank

EMPLOYEE POLICIES

The average number of persons employed by the Group during the year was 1,362 (2005 – 1,260) and the aggregate remuneration paid or payable in respect of the year to those employees was £92,179,000 (2005 – £79,821,000)

The Group encourages staff involvement by a process of communication and consultation. This takes the form of information throughout normal management channels, intranet publications and regular dialogue with staff representatives

All staff are given the opportunity confidentially to state their views about working for the Group via the annual staff opinion survey. Staff are able to comment on a variety of topics from management leadership to communication and employee involvement. The latest survey was undertaken in October 2006. The results of each survey are shared with all staff and action plans are prepared to address the key issues raised.

During 2006, the Group maintained its policy of giving disabled applicants for employment equal consideration to that given to the able for available vacancies, without regard to the difficulties which their disability might cause. The policy also includes the rehabilitation and retention of staff who become disabled, having regard to their particular aptitude and abilities and ensures that disabled staff receive suitable training and development.

DIRECTORS' REPORT (continued)

CHARITABLE CONTRIBUTIONS

During the year, the Group made donations amounting to £832,956 (2005 – £522,088) to United Kingdom charitable organisations. No contributions were made to any political party (2005 – £nil)

POLICY AND PRACTICE ON PAYMENT OF CREDITORS

The Group follows the policy and practice on payment of creditors determined by The Royal Bank of Scotland Group plc (RBSG) as outlined below

RBSG is committed to maintaining a sound commercial relationship with its suppliers. Consequently, it is RBSG's policy to negotiate and agree terms and conditions with its suppliers, which includes the giving of an undertaking to pay suppliers within 30 days of a correctly prepared invoice submitted in accordance with the terms of the contract or such other payment period as may be agreed.

At 31 December 2006, the aggregate amount owed to suppliers represented 17 days (2005 – 15 days) of the amount invoiced by suppliers to the Bank during the year.

AUDITORS

Deloitte & Touche LLP have expressed their willingness to continue in office as auditors and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting on 23 May 2007.

Approved by the Board of Directors
and signed on behalf of the Board



Sally Doyle
Secretary

8
18 April 2007
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STATEMENT OF DIRECTORS' RESPONSIBILITY

The directors are required by the Companies Act 1985 to prepare a directors' report and financial statements for each financial year and have elected to prepare them in accordance with International Financial Reporting Standards as adopted by the European Union. They are responsible for preparing financial statements that present fairly the financial position, financial performance, and cash flows of the Group and the Company. In preparing those financial statements, the directors are required to

- select suitable accounting policies and then apply them consistently,
- make judgements and estimates that are reasonable and prudent, and
- state whether applicable accounting standards have been followed, subject to any material departures disclosed and explained in the accounts

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Company and to enable them to ensure that the directors' report and financial statements comply with the Companies Act 1985. 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.

By order of the Board

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF COUTTS & CO

We have audited the financial statements of Coutts & Co (the "Company") and its subsidiaries (together the "Group") for the year ended 31 December 2006 which comprise the income statement, the balance sheets, the cash flow statements, the statements of changes in equity, the accounting policies and the related notes 1 to 36. These financial statements have been prepared under the accounting policies set out therein.

This report is made solely to the Company's members, as a body, in accordance with section 235 of the Companies Act 1985. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of directors and auditors

As described in the directors' report the Company's directors are responsible for the preparation of the directors' report and financial statements in accordance with applicable law and International Financial Reporting Standards ("IFRSs") as adopted by the European Union. Our responsibility is to audit the financial statements in accordance with relevant legal and regulatory requirements and International Standards on Auditing (UK and Ireland).

We report to you our opinion as to whether the financial statements give a true and fair view and whether the financial statements have been properly prepared in accordance with the Companies Act 1985. We also report to you whether, in our opinion, the information given in the directors' report is consistent with the financial statements. In addition we report to you if, in our opinion, the Company has not kept proper accounting records, if we have not received all the information and explanations we require for our audit, or if information specified by law regarding directors' remuneration and other transactions is not disclosed.

We read the directors' report for the above year and consider whether it is consistent with the audited financial statements. We consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the financial statements. Our responsibilities do not extend to any information outside the directors' report.

Basis of audit opinion

We conducted our audit in accordance with International Standards on Auditing (UK and Ireland) issued by the Auditing Practices Board. An audit includes examination, on a test basis, of evidence relevant to the amounts and disclosures in the financial statements. It also includes an assessment of the significant estimates and judgements made by the directors in the preparation of the financial statements and of whether the accounting policies are appropriate to the circumstances of the Company and the Group, consistently applied and adequately disclosed.

We planned and performed our audit so as to obtain all the information and explanations which we considered necessary in order to provide us with sufficient evidence to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or other irregularity or error. In forming our opinion, we also evaluated the overall adequacy of the presentation of information in the financial statements.

INDEPENDENT AUDITORS' REPORT TO THE MEMBERS OF COUTTS & CO

Opinion

In our opinion

- the financial statements give a true and fair view of the state of the Group's affairs as at 31 December 2006 and of the Group's profit for the year then ended, in accordance with IFRSs as adopted by the European Union,
- the financial statements have been properly prepared in accordance with the Companies Act 1985, and
- the information given in the directors' report is consistent with the financial statements

Separate opinion in relation to IFRS

As explained in Note 1(i), the Group in addition to complying with its legal obligation to comply with IFRSs as adopted by the European Union, has also complied with the IFRSs as issued by the International Accounting Standards Board. Accordingly, in our opinion the financial statements give a true and fair view, in accordance with IFRSs, of the state of the Group's affairs as at 31 December 2006 and of its profit for the year then ended



Deloitte & Touche LLP
Chartered Accountants and Registered Auditors
Stonecutter Court
1 Stonecutter Street
London
EC4A 4TR

16 April 2007

CONSOLIDATED INCOME STATEMENT**Year ended 31 December 2006**

	Notes	2006 £'000	2005 £'000
Interest receivable			
- interest receivable from group undertakings		350,991	296,757
- other interest receivable		243,980	239,324
Interest payable			
- interest payable to group undertakings		(35,438)	(28,728)
- other interest payable		(371,928)	(347,692)
NET INTEREST INCOME		187,605	159,661
Fees and commissions receivable		162,800	131,498
Fees and commissions payable		(6,288)	(5,628)
Income from trading activities	3	13,793	11,728
Other operating income		1	8
NON-INTEREST INCOME		170,306	137,606
TOTAL INCOME		357,911	297,267
Staff costs	4	(113,045)	(98,236)
Premises and equipment		(345)	(5)
Other administrative expenses		(33,864)	(35,611)
Depreciation and amortisation	15,16	(6,101)	(11,423)
Other operating charges	34	(36,816)	(43,616)
Impairment losses on loans and advances	14	(1,429)	64
Provisions for liabilities and charges	23	(2,543)	(600)
OPERATING PROFIT BEFORE TAXATION	6	163,768	107,840
Tax on profit	7	(52,255)	(35,090)
PROFIT FOR THE FINANCIAL YEAR ATTRIBUTABLE TO THE EQUITY HOLDERS OF THE COMPANY		111,513	72,750

CONSOLIDATED BALANCE SHEET
31 December 2006

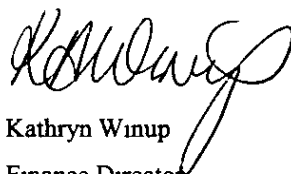
	Notes	2006 £'000	2005 £'000
ASSETS			
Cash and balances at central banks		2,042	1,776
Items in the course of collection from other banks		10,017	43,503
Loans and advances to banks	10	8,587,077	7,215,703
Loans and advances to customers	11	4,451,826	3,842,960
Equity shares	12	12	18
Intangible assets	15	-	1,210
Property, plant and equipment	16	70,570	70,630
Derivatives at fair value	17	3,485	4,738
Other assets, prepayments and accrued income	18	179,033	87,912
TOTAL ASSETS		13,304,062	11,268,450
LIABILITIES			
Deposits by banks	19	862,144	748,112
Items in the course of transmission to other banks		6,933	39,445
Customer accounts	20	11,657,959	9,940,512
Derivatives at fair value	17	2,058	4,705
Other liabilities, accruals and deferred income	21	304,950	171,948
Provisions for liabilities and charges	23	10,446	14,423
Subordinated liabilities			
- loan capital issued by immediate parent undertaking	24	30,933	32,014
TOTAL LIABILITIES		12,875,423	10,951,159
EQUITY			
Shareholders' equity			
Called-up share capital	25	41,333	41,333
Revaluation reserve	26	26,982	26,982
Retained earnings		360,324	248,976
TOTAL EQUITY		428,639	317,291
TOTAL LIABILITIES AND EQUITY		13,304,062	11,268,450

These financial statements were approved by the Board of Directors on 18 April 2007

Signed on behalf of the Board of Directors



The Earl of Home
Chairman



Kathryn Winup
Finance Director

COUTTS & CO

BALANCE SHEET 31 December 2006

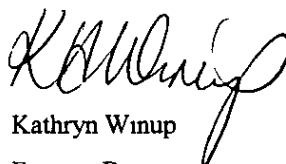
	Notes	2006 £'000	2005 £'000
ASSETS			
Cash and balances at central banks		2,042	1,776
Items in the course of collection from other banks		10,017	43,503
Loans and advances to banks	10	8,587,077	7,220,703
Loans and advances to customers	11	4,431,434	3,822,571
Equity shares	12	12	18
Shares in group undertakings	13	3,350	3,350
Intangible assets	15	-	1,210
Property, plant and equipment	16	70,570	70,630
Derivatives at fair value	17	3,485	4,738
Other assets, prepayments and accrued income	18	178,767	90,265
TOTAL ASSETS		13,286,754	11,258,764
LIABILITIES			
Deposits by banks	19	863,134	748,112
Items in the course of transmission to other banks		6,933	39,445
Customer accounts	20	11,659,631	9,941,032
Derivatives at fair value	17	2,058	4,705
Other liabilities, accruals and deferred income	21	302,292	173,145
Provisions for liabilities and charges	23	10,446	14,423
Subordinated liabilities			
- loan capital issued to immediate parent undertaking	24	30,933	32,014
TOTAL LIABILITIES		12,875,427	10,952,876
EQUITY			
Shareholders' equity			
Called-up share capital	25	41,333	41,333
Revaluation reserve	26	26,982	26,982
Retained earnings		343,012	237,573
TOTAL EQUITY		411,327	305,888
TOTAL LIABILITIES AND EQUITY		13,286,754	11,258,764

These financial statements were approved by the Board of Directors on 18 April 2007

Signed on behalf of the Board of Directors



The Earl of Home
Chairman



Kathryn Winup
Finance Director

CONSOLIDATED STATEMENT OF CHANGES IN EQUITY
31 December 2006

	Notes	Attributable to equity holders of the Group			
		Share capital £'000	Retained earnings £'000	Revaluation reserve £'000	Total £'000
Balance at 31 December 2005		41,333	248,976	26,982	317,291
Changes in equity for 2006					
Profit for the period		-	111,513	-	111,513
Exchange movement		-	(165)	-	(165)
Total recognised income and expense for the period		-	111,348	-	111,348
Balance at 31 December 2006		41,333	360,324	26,982	428,639

	Notes	Attributable to equity holders of the Group			
		Share capital £'000	Retained earnings £'000	Revaluation reserve £'000	Total £'000
Balance at 31 December 2004		41,333	191,951	26,982	260,266
IFRS adjustments (IAS 32 and IAS 39)		-	(3,071)	-	(3,071)
Opening total equity as restated		41,333	188,880	26,982	257,195
Changes in equity for 2005					
Profit for the period		-	72,750	-	72,750
Exchange movement		-	(154)	-	(154)
Total recognised income and expense for the period		-	72,596	-	72,596
Dividends	9	-	(12,500)	-	(12,500)
Balance at 31 December 2005		41,333	248,976	26,982	317,291

STATEMENT OF CHANGES IN EQUITY
31 December 2006

	Notes	Attributable to equity holders of the Company			
		Share capital £'000	Retained earnings £'000	Revaluation reserve £'000	Total £'000
Balance at 31 December 2005		41,333	237,573	26,982	305,888
Changes in equity for 2006					
Profit for the period		-	105,604	-	105,604
Exchange movement		-	(165)	-	(165)
Total recognised income and expense for the period		-	105,439	-	105,439
Balance at 31 December 2006		41,333	343,012	26,982	411,327

		Attributable to equity holders of the Company			
		Share capital £'000	Retained earnings £'000	Revaluation reserve £'000	Total £'000
Balance at 31 December 2004		41,333	185,399	26,982	253,714
IFRS adjustments (IAS 32 and IAS 39)		-	(2,275)	-	(2,275)
Opening total equity as restated		41,333	183,124	26,982	251,439
Changes in equity for 2005					
Profit for the period		-	67,103	-	67,103
Exchange movement		-	(154)	-	(154)
Total recognised income and expense for the period		-	66,949	-	66,949
Dividends	9	-	(12,500)	-	(12,500)
Balance at 31 December 2005		41,333	237,573	26,982	305,888

CONSOLIDATED CASH FLOW STATEMENT
Year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Operating activities			
Group operating profit	29	163,768	107,840
Adjustments for			
Depreciation and amortisation		6,101	11,423
Other non-cash items		(5,247)	2,769
Net cash inflows from trading activities	29	854	14,192
Changes in operating assets	29	(272,801)	(1,134,611)
Changes in operating liabilities	29	1,922,532	1,260,379
Net cash flows from operating activities before tax		1,649,731	125,768
Income taxes paid	29	(43,729)	(35,090)
Cash flows from operating activities		1,770,624	212,710
Investing activities			
Purchase of property, plant and equipment	16	(4,831)	(7,000)
Cash flows from investing activities		(4,831)	(7,000)
Financing activities			
Ordinary equity dividends paid	9	-	(12,500)
Cash flows from financing activities		-	(12,500)
Net increase in cash and cash equivalents		1,765,793	193,210
Cash and cash equivalents 1 January		385,218	192,008
Cash and cash equivalents 31 December	31	2,151,011	385,218

CASH FLOW STATEMENT
Year ended 31 December 2006

	Notes	2006 £'000	2005 £'000
Operating activities			
Banks operating profit	29	155,325	99,320
Adjustments for			
Depreciation and amortisation		6,101	11,423
Other non-cash items		(5,247)	1,814
Net cash inflows from trading activities	29	854	13,237
Changes in operating assets	29	(267,843)	(1,129,727)
Changes in operating liabilities	29	1,923,414	1,262,097
Net cash flows from operating activities before tax		1,655,571	132,370
Income taxes paid	29	(41,126)	(32,217)
Cash flows from operating activities		1,770,624	212,710
Investing activities			
Purchase of property, plant and equipment	16	(4,831)	(7,000)
Cash flows from investing activities		(4,831)	(7,000)
Financing activities			
Ordinary equity dividends paid	9	-	(12,500)
Cash flows from financing activities		-	(12,500)
Net increase in cash and cash equivalents		1,765,793	193,210
Cash and cash equivalents 1 January		385,218	192,008
Cash and cash equivalents 31 December	31	2,151,011	385,218

NOTES TO THE ACCOUNTS
Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES

(i) Adoption of International Financial Reporting Standards

The consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (IFRS) adopted by the International Accounting Standards Board (IASB), and interpretations issued by the International Financial Reporting Interpretations Committee of the IASB. The date of transition to IFRS for the Group and the date of its opening IFRS balance sheet was 1 January 2004. On initial adoption of IFRS, the Group applied the following exemptions from the requirements of IFRS and from their retrospective application as permitted by IFRS 1 'First-time Adoption of International Financial Reporting Standards' (IFRS 1):

Fair value or revaluation as deemed cost – under UK Generally Accepted Accounting Practices ("UK GAAP"), the Group's freehold and long leasehold property occupied for its own use was recorded at valuation on the basis of existing use value. The Group has elected to use this valuation as at 31 December 2003 as deemed cost for its opening IFRS balance sheet. At this date, the carrying value under UK GAAP of freehold and long leasehold property occupied for own use was £48,802,000.

Derecognition – the Group has applied the derecognition requirements of IAS 39 to transactions occurring on or after 1 January 1992.

Share based payments – IFRS 2 'Share-based Payment' has been applied by The Royal Bank of Scotland Group plc to equity instruments granted after 7 November 2002. The Group receives a recharge from The Royal Bank of Scotland Group plc in relation to these payments.

The Group has adopted the Amendment to IAS 39 'The Fair Value Option' issued by the IASB in June 2005 with effect from 1 January 2005.

(ii) Accounting convention

The financial statements have been prepared on the historical cost basis except that the following assets and liabilities are stated at their fair value: derivative financial instruments and financial assets and financial liabilities.

(iii) Basis of consolidation

The consolidated financial statements incorporate the financial statements of the holding company (Coutts & Co) and its subsidiaries. Control exists where the Group has the power to govern the financial and operating policies of the entity, generally conferred by holding a majority of voting rights.

All intra-group balances, transactions, income and expenses are eliminated on consolidation. The consolidated accounts are prepared using uniform accounting policies.

NOTES TO THE ACCOUNTS (continued)

Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES (continued)

(iv) Revenue Recognition

Interest income on financial assets that are classified as loans and receivables and interest expense on financial liabilities other than those at fair value through profit or loss is determined using the effective interest method. The effective interest method is a method of calculating the amortised cost of a financial asset or financial liability (or group of financial assets or liabilities) and of allocating the interest income or interest expense over the expected life of the asset or liability. The effective interest rate is the rate that exactly discounts estimated future cash flows to the instrument's initial carrying amount. Calculation of the effective interest rate takes into account fees receivable, that are an integral part of the instrument's yield, premiums or discounts on acquisition or issue, early redemption fees and transaction costs. All contractual terms of a financial instrument are considered when estimating future cash flows.

Financial assets and financial liabilities held for trading and financial liabilities designated as fair value through profit or loss are recorded at fair value. Changes in fair value are recognised in profit or loss together with dividends and interest receivable and payable.

Commitment and utilisation fees are determined as a percentage of the outstanding facility. If it is unlikely that a specific lending arrangement will be entered into, such fees are taken to profit or loss over the life of the facility; otherwise they are deferred and included in the effective interest rate on the advance.

Fees in respect of services are recognised as the right to consideration accrues through the provision of the service to the customer. The arrangements are generally contractual and the cost of providing the service is incurred as the service is rendered. The price is usually fixed and always determinable. The application of this policy to significant fee types is outlined below.

Payment services this comprises income received for payment services including cheques cashed, direct debits, Clearing House Automated Payments (the UK electronic settlement system) and BACS payments (the automated clearing house that processes direct debits and direct credits). These are generally charged on a per transaction basis. The income is earned when the payment or transaction occurs. Payment services income is usually charged to the customer's account, monthly or quarterly in arrears. Accruals are raised for services provided but not charged at period end.

Card related services fees from credit card business include commission received from retailers for processing credit and debit card transactions. Income is accrued to the income statement as the service is performed.

Interchange received as issuer, the Group receives a fee (interchange) each time a cardholder purchases goods and services. The Group also receives interchange fees from other card issuers for providing cash advances through its branch and Automated Teller Machine networks. These fees are accrued once the transaction has taken place.

Investment management fees fees charged for managing investments are recognised as revenue as the services are provided. Incremental costs that are directly attributable to securing an investment management contract are deferred and charged as expense as the related revenue is recognised.

NOTES TO THE ACCOUNTS (continued)**Year ended 31 December 2006****1. PRINCIPAL ACCOUNTING POLICIES (continued)****(v) Pensions and other post-retirement benefits**

The Royal Bank of Scotland Group plc provides post-retirement benefits in the form of pensions and healthcare plans to eligible employees. The cost of defined benefit pension schemes and healthcare plans is assessed by independent professionally qualified actuaries and recognised on a systematic basis over employees' service lives.

For defined benefit schemes, scheme liabilities are measured on an actuarial basis using the projected unit credit method and discounted at a rate that reflects the current rate of return on a high quality corporate bond of equivalent term and currency to the scheme liabilities. Scheme assets are measured at their fair value. Any surplus or deficit of scheme assets over liabilities is recognised in the balance sheet as an asset (surplus) or liability (deficit). The current service cost and any past service costs together with the expected return on scheme assets less the unwinding of the discount on the scheme liabilities is charged to operating expenses. Actuarial gains and losses are recognised in full in the period in which they occur outside profit or loss and presented in the statement of recognised income and expense.

There is no contractual agreement or policy on the way that the cost of The Royal Bank of Scotland Group plc defined benefit pension schemes and healthcare plans are allocated to the Group. It therefore accounts for the charges it incurs as payments to a defined contribution scheme.

There is no defined contribution pension scheme.

(vi) Intangible asset

The intangible asset that was acquired by the Group is stated at cost less accumulated amortisation and impairment losses. Amortisation is charged to profit or loss using methods that best reflect the economic benefits over their estimated useful economic life and included in depreciation and amortisation. The estimated useful economic life is as follows:

Computer software development costs	3 years
-------------------------------------	---------

(vii) Property, plant and equipment

Items of property, plant and equipment are stated at cost less accumulated depreciation (see below) and impairment losses. Where an item of property, plant and equipment comprises major components having different useful lives, they are accounted for separately.

Depreciation is charged to profit or loss on a straight-line basis so as to write off the depreciable amount of property, plant and equipment over their estimated useful lives. The depreciable amount is the cost of an asset less its residual value. Estimated useful lives are as follows:

Freehold and long leasehold buildings	50 years
Short leaseholds	unexpired period of the lease
Property adaptation costs	10 years
Computer equipment	5 years
Motor vehicles	5 years
Other plant and equipment	10 to 15 years

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES (continued)

(viii) Impairment of intangible assets and property, plant and equipment

At each reporting date, the Group assesses whether there is any indication that its intangible assets or property, plant and equipment are impaired. If any such indication exists, the Group estimates the recoverable amount of the asset and the impairment loss if any. Irrespective of any indications of impairment, intangible assets with indefinite useful lives are tested annually for impairment by comparing their carrying value with their recoverable amount. If an asset does not generate cash flows that are independent from those of other assets or groups of assets, recoverable amount is determined for the cash-generating unit to which the asset belongs. The recoverable amount of an asset is the higher of its fair value less costs to sell and its value in use. Value in use is the present value of future cash flows from the asset or cash-generating unit discounted at a rate that reflects market interest rates adjusted for risks specific to the asset or cash-generating unit that have not been reflected in the estimation of future cash flows. If the recoverable amount of an intangible or tangible asset is less than its carrying value, an impairment loss is recognised immediately in profit or loss and the carrying value of the asset reduced by the amount of the loss. A reversal of an impairment loss on intangible assets or property, plant and equipment is recognised as it arises provided the increased carrying value does not exceed that which it would have been had no impairment loss been recognised.

(ix) Foreign currencies

The Group's consolidated financial statements are presented in sterling which is the functional currency of the Company.

Transactions in foreign currencies are translated into sterling at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into sterling at the rates of exchange ruling at the balance sheet date. Foreign exchange differences arising on translation are recognised in profit or loss.

The assets and liabilities of foreign operations are translated into sterling at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of foreign operations are translated into sterling at average exchange rates unless these do not approximate to the foreign exchange rates ruling at the dates of the transactions. Foreign exchange differences arising on translation of foreign operations are recognised directly in equity.

(x) Leases

Contracts to lease assets are classified as finance leases if they transfer substantially all the risks and rewards of ownership of the asset to the customer. Other contracts to lease assets are classified as operating leases. All the Group's leases are accounted for as operating leases.

Rental income from operating leases is credited to the income statement on a receivable basis over the term of the lease. Operating lease assets are included within property, plant and equipment and depreciated over their useful lives (see note vii).

(xi) Taxation

Provision is made for taxation at current enacted rates on taxable profits, arising in income or in equity, taking into account relief for overseas' taxation where appropriate. Deferred taxation is accounted for in full for all temporary differences between the carrying amount of an asset or liability for accounting purposes and its carrying amount for tax purposes, except in relation to overseas' earnings where remittance is controlled by the Group.

Deferred tax assets are only recognised to the extent that it is probable that they will be recovered.

NOTES TO THE ACCOUNTS (continued)

Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES (continued)

(xii) Financial assets

Financial assets are classified as loans and receivables, available for sale and held for trading

Loans and receivables – non-derivative financial assets with fixed or determinable repayments that are not quoted in an active market are classified as loans and receivables. Loans and receivables are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at adjusted cost using the effective interest method less any impairment losses.

Held for trading – a financial asset is classified as held for trading if it is acquired principally for the purpose of the selling in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative. Held for trading financial assets are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses on held for trading financial assets are recognised in profit or loss as they arise.

Available for sale – financial assets that are not classified as loans and receivables or held for trading are classified as available for sale. Financial assets can be designated as available for sale on initial recognition. Available for sale financial assets are initially recognised at fair value plus directly related transaction costs. They are subsequently measured at fair value. Changes in the fair value of available for sale financial assets are reported in a separate component of shareholders' equity. Interest calculated using the effective interest rate (see note 14 above) is recognised in profit or loss.

On implementation of IAS 39, no financial assets were designated at fair value through profit or loss.

Regular way purchases of financial assets classified as loans and receivables are recognised on settlement date, all other regular way purchases are recognised on trade date. Fair value for a net open position in a financial asset that is quoted in an active market is the current bid price times the number of units of the instrument held. Fair values for financial assets not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial assets.

(xiii) Impairment of financial assets

The Group assesses at each balance sheet date whether there is any objective evidence that a financial asset or group of financial assets classified as loans and receivables or available for sale is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset.

Financial assets carried at amortised cost - if there is objective evidence that an impairment loss on a financial asset or group of financial assets classified as loans and receivables has been incurred, the Group measures the amount of the loss as the difference between the carrying amount of the asset or group of assets and the present value of estimated future cash flows from the asset or group of assets discounted at the effective interest rate of the instrument at initial recognition. Impairment losses are assessed individually for financial assets that are individually significant. Historical loss experience is adjusted, on the basis of current observable data, to reflect the effects of current conditions not affecting the period of historical experience.

Impairment losses are recognised in profit or loss and the carrying amount of the financial asset or group of financial assets reduced by establishing an allowance for impairment losses. If in a subsequent period the amount of the impairment loss reduces and the reduction can be ascribed to an event after the impairment was recognised, the previously recognised loss is reversed by adjusting the allowance. Once an impairment loss has been recognised on a financial asset or group of financial assets, interest income is recognised on the carrying amount using the rate of interest at which estimated future cash flows were discounted in measuring impairment.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES (continued)

(xiii) Impairment of financial assets (continued)

Financial assets carried at fair value – when a decline in the fair value of a financial asset classified as available for sale has been recognised directly in equity and there is objective evidence that the asset is impaired, the cumulative loss is removed from equity and recognised in profit or loss. The loss is measured as the difference between the amortised cost of the financial asset and its current fair value. Impairment losses on available for sale equity instruments are not reversed through profit or loss.

(xiv) Financial liabilities

Financial liabilities are measured at amortised cost using the effective interest method (see note iv above) or fair value.

A financial liability is classified as held for trading if it is incurred principally for the purpose of selling in the near term, or forms part of a portfolio of financial instruments that are managed together and for which there is evidence of short-term profit taking, or it is a derivative. Held for trading financial liabilities are recognised at fair value with transaction costs being recognised in profit or loss. Subsequently they are measured at fair value. Gains and losses are recognised in profit or loss as they arise. Financial liabilities that the Group designates on initial recognition as being at fair value through profit or loss are recognised at fair value with transaction costs being recognised in profit or loss and are subsequently measured at fair value. Gains and losses on financial liabilities that are designated at fair value through profit or loss are recognised in profit or loss as they arise. Financial liabilities may be designated at fair value through profit or loss only if such designation relates to an instrument that contains an embedded derivative which is not evidently closely related to the host contract. All other financial liabilities are measured at amortised cost using the effective interest method (see note iv above).

Fair value for a net open position in a financial liability that is quoted in an active market is the current offer price times the number of units of the instrument held or issued. Fair values for financial liabilities not quoted in an active market are determined using appropriate valuation techniques including discounting future cash flows, option pricing models and other methods that are consistent with accepted economic methodologies for pricing financial liabilities.

(xv) Derivatives

Derivative financial instruments are recognised initially, and subsequently measured, at fair value. Derivative fair values are determined from quoted prices in active markets where available. Where there is no active market for an instrument, fair value is derived from prices for the derivative's components using appropriate pricing or valuation models.

A derivative embedded in a contract is accounted for as stand-alone derivative if its economic characteristics are not closely related to the economic characteristics of the host contract, unless the entire contract is carried at fair value through profit or loss.

Gains and losses arising from changes in fair value of a derivative are recognised as they arise in profit or loss.

(xvi) Share-based payments

The Royal Bank of Scotland Group plc grants options over shares to its employees under various share option schemes. IFRS 2 'Share-based Payment' is applied by The Royal Bank of Scotland Group plc to grants under these schemes after 7 November 2002 that had not vested on 1 January 2007. The Royal Bank of Scotland Group plc recognises an expense for these transactions with its employees based on the fair value on the date the options are granted. It includes the cost of these awards in determining any recharges of employee costs it makes to UK subsidiaries in the Group.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

1. PRINCIPAL ACCOUNTING POLICIES (continued)

(xvii) Cash and cash equivalents

Cash and cash equivalents comprises cash on hand and demand deposits with banks together with short-term highly liquid investments that are readily convertible to known amounts of cash and subject to insignificant risk of changes in value

(xviii) Related Party Transactions

IFRS requires all entities to disclose related party transactions. The company's policy is to have regard to materiality from the shareholder's perspective

(xix) Offsetting

Financial assets and financial liabilities are only offset and the net amount reported in the balance sheet when there is a legally enforceable right to set off the recognised amounts and the Group intends either to settle on a net basis or to realise the asset and settle the liability simultaneously

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The reported results of the Group for 2006 are sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. The Group's principal accounting policies are set out on pages 16 to 22. UK company law and IFRS require the directors, in preparing the Group's financial statements, to select suitable accounting policies, apply them consistently and make judgements and estimates that are reasonable and prudent. In the absence of an applicable standard of interpretation, International Accounting Standard ("IAS") 8 'Accounting Policies, Changes in Accounting Estimates and Errors' requires management to develop and apply an accounting policy that results in relevant and reliable information in the light of the requirements and guidance in IFRS dealing with similar and related issues and the IASB's Framework for the Preparation and Presentation of Financial Statements.

The judgements and assumptions involved in the Group's accounting policies that are considered by the Board to be the most important to the portrayal of its financial condition are discussed below. The use of estimates, assumptions or models that differ from those adopted by the Group would affect its reported results.

(i) Impairment provisions – financial assets

The Group's loan impairment provisions are established to recognise incurred impairment losses in its portfolio of loans classified as loans and receivables and carried at amortised cost. A loan is impaired where there is objective evidence that events since the loan was granted have affected expected cash flows from the loan. The impairment loss is the difference between the carrying value of the loan and the present value of estimated future cash flows at the loan's original effective interest rate.

There are two components to the Group's loan impairment provisions: individual and collective.

Individual component – all impaired loans are individually assessed for impairment. Impairment losses are recognised as the difference between the carrying value of the loan and the discounted value of management's best estimate of future cash repayments and proceeds from any security held. These estimates take into account the customer's debt capacity and financial flexibility, the level and quality of its earnings, the amount and sources of cash flows, the industry in which the counterparty operates, and the realisable value of any security held. Estimating the quantum and timing of future recoveries involves significant judgement. The size of receipts will depend on the future performance of the borrower and the value of security, both of which will be affected by future economic conditions; additionally, collateral may not be readily marketable. The actual amount of future cash flows and the date they are received may differ from these estimates and consequently actual losses incurred may differ from those recognised in these financial statements.

Collective component – this is made up of loan losses that have been incurred but have not been separately identified at the balance sheet date (latent loss provisions). The methodology by which the Latent Loss Reserve is calculated entails a statistical estimation of existing but unidentified defaults, based upon the level of identified individual impairments and the emergence period (the average time taken for current impaired loans to be recognised and provided for under the individual impairment assessment process).

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

2. CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS (continued)

(ii) Fair value

Financial instruments classified as held for trading and financial assets classified as available for sale are recognised in the financial statements at fair value. All derivatives are measured at fair value. In the balance sheet, financial assets carried at fair value are included within Loans and Advances to Banks, Loans and Advances to Customers and Equity shares as appropriate. Financial liabilities carried at fair value are included within the captions Deposits by Banks, Customer Accounts and Subordinated Liabilities as appropriate. Derivative assets and Derivative liabilities are shown separately on the face of the balance sheets. Gains or losses arising from changes in fair value of financial instruments classified as held for trading are included in the income statement. Unrealised gains and losses on available for sale financial assets are recognised directly in equity, unless an impairment loss is recognised.

Fair value is the amount for which an asset could be exchanged, or a liability settled, between knowledgeable, willing parties in an arm's length transaction. Fair values are determined by reference to observable market prices where available and reliable. Where representative market prices for an instrument are not available or are unreliable because of poor liquidity, the fair value is derived from prices for its components using appropriate pricing or valuation models that are based on independently sourced market parameters, including interest rate yield curves, option volatilities and currency rates.

The Group's derivative products include swaps, forwards, futures and options. Exchange traded instruments are valued using quoted prices. The fair value of over-the-counter instruments is derived from pricing models which take account of contract terms, including maturity, as well as quoted market parameters such as interest rates and volatilities. Most of the Group's pricing models do not entail material subjectivity because the methodologies utilised do not incorporate significant judgement and the parameters included in the models can be calibrated to actively quoted market prices. Values established from pricing models are adjusted for credit risk, liquidity risk and future operational costs.

A negligible proportion of the Group's trading derivatives are valued directly from quoted prices, the majority being valued using appropriate valuation techniques. The fair value of substantially all securities' positions carried at fair value is determined directly from quoted prices.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

3. INCOME FROM TRADING ACTIVITIES

	2006	2005
	£'000	£'000
Foreign exchange	13,793	11,728

Foreign exchange includes spot and forward foreign exchange contracts, interest rate swaps, currency swaps, futures and options

4. STAFF COSTS

	2006	2005
	£'000	£'000
Staff costs		
Wages and salaries	92,179	79,821
Social security costs	8,878	7,479
Pension costs (see note 5)	11,988	10,936
	<u>113,045</u>	<u>98,236</u>

The average number of persons employed by the Group and the Bank during the year was made up as follows

	Number of Employees	
	2006	2005
Managers	556	542
Clerical and other staff	806	718
	<u>1,362</u>	<u>1,260</u>

5. PENSION COSTS

Members of the Group sponsor a number of pension schemes in the UK and overseas, predominantly of the defined benefit type, whose assets are independent of the Group's finances. Defined benefit pensions generally provide a pension of one sixtieth of final pensionable salary for each year of service prior to retirement. Employees do not make contributions for basic pensions but can make voluntary contributions to secure additional benefits on a money-purchase basis. Since October 2006 The Royal Bank of Scotland Group Pension Fund ('Main Scheme') has been closed to new entrants. The Group also provides other post-retirement benefits, principally through subscriptions to private healthcare schemes in the UK and the US and unfunded post-retirement benefit plans. Provision for the costs of these benefits is charged to the income statement over the average remaining future service lives of eligible employees. The amounts are not material.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

5. PENSION COSTS (continued)

Interim valuations of the Group's schemes were prepared to 31 December by independent actuaries, using the following assumptions

Principal actuarial assumptions at 31 December	Main scheme		2004
	2006	2005	
Discount rate	5.3%	4.8%	5.4%
Expected return on plan assets (weighted average)	6.9%	6.5%	6.7%
Rate of increase in salaries	4.2%	4.0%	4.0%
Rate of increase in pensions in payment	2.9%	2.7%	2.7%
Inflation assumption	2.9%	2.7%	2.7%

Major classes of plan assets as a percentage of total plan assets	Main scheme		2004
	2006	2005	
Equities	60.5%	61.3%	56.7%
Index-linked bonds	17.3%	18.1%	16.5%
Government fixed interest bonds	2.5%	1.8%	2.1%
Corporate and other bonds	14.0%	14.6%	12.5%
Property	4.3%	3.6%	3.1%
Cash and other assets	1.4%	0.6%	9.1%

Ordinary shares of the Company with a fair value of £89 million (2005 - £78 million, 2004 - £73 million), are held by the Group's pension schemes, £87 million (2005 - £76 million, 2004 - £71 million) in the Main scheme which also holds other financial instruments issued by the Group with a value of £258 million (2005 - £299 million, 2004 - £726 million)

The expected return on plan assets at 31 December is based upon the weighted average of the following assumed returns on the major classes of plan assets

	Main scheme		2004
	2006	2005	
Equities	8.1%	7.7%	8.1%
Index-linked bonds	4.5%	4.1%	4.5%
Government fixed interest bonds	4.5%	4.1%	4.5%
Corporate and other bonds	5.3%	4.8%	5.4%
Property	6.3%	5.9%	6.3%
Cash and other assets	4.6%	4.2%	4.6%

The expected return on Main scheme assets at 31 December 2004 was adjusted to reflect the investment, in early January 2005, of payments made to the fund on 31 December 2004 and included as cash and other assets at that date

Post-retirement mortality assumptions (Main scheme)	2006	2005	2004
<i>Longevity at age 60 for current pensioners (years)</i>			
Males	26.0	25.4	25.4
Females	28.9	28.2	28.2
<i>Longevity at age 60 for future pensioners (years)</i>			
Males	26.8	26.2	26.2
Females	29.7	29.0	29.0

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

5. PENSION COSTS (continued)

	Main scheme					
	Fair value of plan assets £m	2006 Present value of defined benefit obligations £m	Net pension liability £m	Fair value of plan assets £m	2005 Present value of defined benefit obligations £m	Net pension liability £m
At 1 January	15,914	19,118	3,204	13,569	16,051	2,482
Income Statement						
Expected return	1,022	-	(1,022)	930	-	(930)
Interest cost	-	918	918	-	865	865
Current service cost	-	571	571	-	447	447
Past service cost	-	15	15	-	3	3
	<u>1,022</u>	<u>1,504</u>	<u>482</u>	<u>930</u>	<u>1,315</u>	<u>385</u>
Statement of recognised income and expense						
Actuarial gains and losses	552	(1,077)	(1,629)	1,556	2,273	717
Contributions by employer	427	-	(427)	380	-	(380)
Benefits paid	(515)	(515)	-	(504)	(504)	-
Expenses included in service cost	(26)	(26)	-	(17)	(17)	-
	<u>17,374</u>	<u>19,004</u>	<u>1,630</u>	<u>15,914</u>	<u>19,118</u>	<u>3,204</u>
At 31 December						

The Group expects to contribute £464 million to its defined benefit pension schemes in 2007 (Main Scheme - £408 million). Of the net pension liability, £106 million (2005 - £104 million) relates to unfunded schemes.

Cumulative net actuarial losses of £619 million (2005 - £2,400 million, 2004 - £1,601 million) have been recognised in the statement of recognised income and expense, of which £521 million (2005 - £2,150 million, 2004 - £1,433 million) relate to the Main scheme.

	Main scheme			
	2006 £m	2005 £m	2004 £m	2003 £m
History of defined benefit schemes				
Present value of defined benefit obligations	19,004	19,118	16,051	13,594
Fair value of plan assets	17,374	15,914	13,569	11,797
Net deficit	1,630	3,204	2,482	1,797
Experience losses on plan liabilities	(4)	(41)	(624)	
Experience gains on plan assets	552	1,556	392	
Actual return on pension scheme assets	1,574	2,486	1,230	

NOTES TO THE ACCOUNTS (continued)

Year ended 31 December 2006

6. OPERATING PROFIT BEFORE TAXATION

	2006 £'000	2005 £'000
Operating profit for the year is stated after crediting:		
Aggregate amounts receivable under operating leases	2,514	1,904
And after charging:		
Interest payable in respect of subordinated liabilities	1,438	1,483
Aggregate amounts payable under land and building operating leases	2,083	1,944
Auditors' remuneration		
- audit of the Bank	227	220
- audit of subsidiaries	10	10
Fees paid to auditors for non-audit work	45	36

7. TAX ON OPERATING PROFIT

	2006 £'000	2005 £'000
Current taxation		
United Kingdom corporation tax at 30% (2005 – 30%)	50,966	31,915
Under provision in respect of prior periods	1,297	2,334
	52,263	34,249
Deferred taxation		
Origination and reversal of timing differences	(395)	1,599
Under/(over) provision in respect of prior periods	387	(758)
	52,255	35,090

The actual tax charge differs from the expected tax charge computed by applying the standard rate of UK corporation tax of 30% as follows

	The Group	
	2006 £'000	2005 £'000
Expected tax charge	49,130	32,352
Factors affecting charge:		
Disallowable expenses	1067	1527
Depreciation in (deficit)/excess of capital allowances	(168)	(705)
Non-qualifying depreciation	937	(1,259)
Prior year adjustments	1,289	3,175
Tax charge for the year	52,255	35,090

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

8. PROFIT DEALT WITH IN THE ACCOUNTS OF THE BANK

As permitted by Section 230 of the Companies Act 1985, the profit of the Bank has not been presented separately. Profit after tax of £105,604,000 (2005 - £67,103,000) for the financial year has been dealt with in the accounts of the Bank (page 12)

9. DIVIDENDS

	2006	2006	2005	2005
	Pence per		Pence per	
	share	£'000	share	£'000
Interim	-	-	0.3024	12,500

10. LOANS AND ADVANCES TO BANKS

	The Bank		The Group	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Loans and receivables	8,589,041	7,222,667	8,589,041	7,217,667
Individual impairment provision (note 14)	(1,964)	(1,964)	(1,964)	(1,964)
	<u>8,587,077</u>	<u>7,220,703</u>	<u>8,587,077</u>	<u>7,215,703</u>
Amounts include				
Due from RBS Group undertakings	<u>8,583,718</u>	<u>7,205,815</u>	<u>8,583,718</u>	<u>7,200,815</u>

11. LOANS AND ADVANCES TO CUSTOMERS

	The Bank		The Group	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Loans and receivables	4,449,156	3,841,505	4,469,548	3,861,951
Individual and collective impairment provision (note 14)	(17,722)	(18,934)	(17,722)	(18,991)
	<u>4,431,434</u>	<u>3,822,571</u>	<u>4,451,826</u>	<u>3,842,960</u>
Amounts include				
Due from subsidiary undertakings	<u>1,049,291</u>	<u>945,144</u>		

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

12. EQUITY SHARES

	The Bank and The Group			
	2006	2006	2005	2005
	Balance	Fair	Balance	Fair
	sheet	value	sheet	value
	£'000	£'000	£'000	£'000
Investment securities				
Available for sale - unlisted	12	12	18	18
			Equity holding	
			2006	2005
			%	%

The principal equity shares are
Voca Limited £1 Shares

0 06 0 07

The fair value of the investments in Voca Limited (formerly BACS Limited) is based upon the value attributed to each share when Voca Limited completed a shareholding realignment in May 2004. There is no active market for these shares.

13. SHARES IN GROUP UNDERTAKINGS

	2006	2005
	£'000	£'000
The Bank		
Subsidiary undertakings		
Cost and carrying value at 1 January and 31 December	3,350	3,350

The Bank owns 100% of the ordinary share capital and voting rights of Coutts Finance Co, 440 Strand, London WC2R 0QS, which is an unlisted company incorporated in Great Britain and registered in England and Wales. Its principal business is the provision of residential mortgages in the United Kingdom.

The Bank owns 100% of the ordinary share capital and voting rights of Coutts & Co Investment Management Limited, 440 Strand, London WC2R 0QS, which is an unlisted company incorporated in Great Britain and registered in England and Wales. Its principal business is the provision of investment management services to residents of the United States.

Other wholly owned subsidiary undertakings are unlisted dormant companies used mainly for nominee purposes, all of which are incorporated in Great Britain and registered in England and Wales.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

14. IMPAIRED FINANCIAL ASSETS

	2006	2005
	£'000	£'000
Impairment losses charged /(released) to profit or loss		
The Group		
Loans and receivables		
Loans and advances (see table below)	1,429	(64)
	<hr/>	<hr/>
Total	<u>1,429</u>	<u>(64)</u>

The following table shows impairment provisions for loans and advances classified as loans and receivables

	2006	2005
	Total	Total
	£'000	£'000
The Group		
At 1 January	20,955	27,959
Implementation of IAS 39	-	(3,835)
Amounts written off	(1,677)	(1,821)
Charge/ (release) to profit and loss	1,429	(64)
Unwind of discount	(1,021)	(1,284)
	<hr/>	<hr/>
At 31 December	<u>19,686</u>	<u>20,955</u>
	<hr/>	<hr/>
Loans and advances to banks	1,964	1,964
Loans and advances to customers	17,722	18,991
	<hr/>	<hr/>
Group total	<u>19,686</u>	<u>20,955</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

14. IMPAIRED FINANCIAL ASSETS (continued)

	2006	2005
	£'000	£'000
Impairment losses charged to profit or loss		
The Bank		
Loans and receivables		
Loans and advances (see table below)	1,486	891
	<hr/>	<hr/>
Total	1,486	891
	<hr/>	<hr/>

The following table shows impairment provisions for loans and advances classified as loans and receivables

	2006	2005
	Total	Total
	£'000	£'000
The Bank		
At 1 January	20,898	26,947
Implementation of IAS 39	-	(3,835)
Amounts written off	(1,677)	(1,821)
Charge to profit and loss	1,486	891
Unwind of discount	(1,021)	(1,284)
	<hr/>	<hr/>
At 31 December	19,686	20,898
	<hr/>	<hr/>
Loans and advances to banks	1,964	1,964
Loans and advances to customers	17,722	18,934
	<hr/>	<hr/>
Bank total	19,686	20,898
	<hr/>	<hr/>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

15. INTANGIBLE FIXED ASSETS

The Bank and The Group	Software £'000
Cost	
At 1 January 2006 and 31 December 2006	20,129
Accumulated amortisation and impairment	
At 1 January 2006	18,919
Charge for the year	1,210
	<hr/>
At 31 December 2006	20,129
	<hr/>
Net book value at 31 December 2006	-
	<hr/>
Net book value at 31 December 2005	1,210
	<hr/>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

16. PROPERTY, PLANT AND EQUIPMENT

The Bank & The Group	Freehold land and buildings £'000	Principal office long leasehold £'000	Long leasehold £'000	Short leasehold £'000	Computers and other equipment £'000	Total £'000
Cost or valuation						
At 1 January 2006	6,581	69,818	3,502	11,252	17,359	108,512
Additions	29	3,333	(219)	1,261	427	4,831
Disposals	-	-	-	-	(28)	(28)
At 31 December 2006	6,610	73,151	3,283	12,513	17,758	113,315
Depreciation						
At 1 January 2006	949	18,760	1,003	5,131	12,039	37,882
Charge for the year	157	1,425	122	1,354	1,833	4,891
Disposals	-	-	-	-	(28)	(28)
At 31 December 2006	1,106	20,185	1,125	6,485	13,844	42,745
Net book value						
At 31 December 2006	5,504	52,966	2,158	6,028	3,914	70,570
At 31 December 2005	5,632	51,058	2,499	6,121	5,320	70,630

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

17. DERIVATIVES AT FAIR VALUE

	2006			2005		
	Notional amounts	Total derivatives Assets	Liabilities	Notional amounts	Total derivatives Assets	Liabilities
The Bank & the Group	£'000	£'000	£'000	£'000	£'000	£'000
Exchange rate related contracts						
Forward foreign exchange	124,098	1,821	1,738	185,257	1,117	1,075
Free standing derivatives						
Interest rate contracts						
Interest rate swaps	191,232	1,664	320	926,152	3,621	3,630
	<u>315,330</u>	<u>3,485</u>	<u>2,058</u>	<u>1,111,409</u>	<u>4,738</u>	<u>4,705</u>

18. OTHER ASSETS, PREPAYMENTS AND ACCRUED INCOME

	The Bank		The Group	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Taxation	-	3,348	-	741
Deferred Taxation (note 22)	6,618	7,599	6,618	7,599
Other assets				
- RBS Group undertakings	142,173	51,872	142,173	51,872
- other	2,656	2,192	2,656	2,192
Other prepayments and accrued income				
- RBS Group undertakings	6,408	-	6,674	-
- other	20,912	25,254	20,912	25,508
	<u>178,767</u>	<u>90,265</u>	<u>179,033</u>	<u>87,912</u>

19. DEPOSITS BY BANKS

	The Bank		The Group	
	2006 £'000	2005 £'000	2006 £'000	2005 £'000
Amortised cost	863,134	748,112	862,144	748,112
Amounts include				
Due to RBS Group undertakings	854,995	741,563	853,185	741,563

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

20. CUSTOMER ACCOUNTS

	The Bank		The Group	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Amortised cost	11,659,631	9,941,032	11,657,959	9,940,512

The Bank holds deposits from its subsidiary undertakings Included within the above are deposits from subsidiary undertakings of £1,672,000 (2005 - £521,000)

21. OTHER LIABILITIES, ACCRUALS AND DEFERRED INCOME

	The Bank		The Group	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Taxation	4,267	-	6,804	-
Payables and accrued expenses				
- RBS Group undertakings	249,564	132,999	249,564	132,183
- other	1,867	1,413	1,867	1,413
Other accruals and deferred income				
- other	46,594	38,733	46,715	38,352
	<u>302,292</u>	<u>173,145</u>	<u>304,950</u>	<u>171,948</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

22. DEFERRED TAXATION

	The Group		
	Accelerated capital allowances	Other timing differences	Total
	£'000	£'000	£'000
At 1 January 2005	392	(8,832)	(8,440)
Charge to income statement	1,009	(168)	841
At 31 December 2005	1,401	(9,000)	(7,599)
Charge to income statement	710	271	981
At 31 December 2006	2,111	(8,729)	(6,618)

	The Bank		
	Accelerated capital allowances	Other timing differences	Total
	£'000	£'000	£'000
At 1 January 2005	392	(8,492)	(8,100)
Charge to income statement	1,009	(508)	501
At 31 December 2005	1,401	(9,000)	(7,599)
Charge to income statement	710	271	981
At 31 December 2006	2,111	(8,729)	(6,618)

The provision for UK deferred taxation has been calculated at 30% (2005 – 30%), being the rate of corporation tax. A deferred tax asset of £6,618,000 has been recognised at 31 December 2006 (2005 – £7,599,000). This asset has been recognised in the financial statements following the deferral of bonuses under the medium term incentive plan, the provision for litigation and sundry losses, the impairment provision and accelerated capital allowances. The directors are of the opinion, based on recent and forecasted trading, that the level of profits in the current and next financial year will exceed the value of the deferred tax asset. There is no unprovided potential deferred taxation liability (2005 - £Nil), particularly in respect of revaluation gains on properties.

NOTES TO THE ACCOUNTS (continued)**Year ended 31 December 2006****22. DEFERRED TAXATION (continued)**

The directors are of the opinion that, in view of the type and use of properties involved, the likelihood of any material tax liabilities arising on the disposal of the Group's properties at current market value is so remote that no useful purpose would be served in attempting to quantify it. Most of the Group's properties are occupied for the purposes of the Group's trade and consequently any gains arising on disposal are normally rolled-over pursuant to Taxation of Chargeable Gains Act 1992, Section 152.

23. PROVISIONS FOR LIABILITIES AND CHARGES

	The Bank & The Group			
	Provision for severance (1) £'000	Provision for MTIP (2) £'000	Other provisions (3) £'000	Total provisions £'000
Provision as at 1 January 2006	2,931	9,192	2,300	14,423
Charged to the profit and loss	100	2,732	-	2832
Released during the year	(289)	-	-	(289)
	(189)	2,732	-	2,543
Utilised in year	(1,948)	(4,572)	-	(6,520)
Provision as at 31 December 2006	794	7,352	2,300	10,446

Notes

- (1) The Group provides for future severance costs where there is a constructive obligation arising within the next 12 months
- (2) The Group operates Medium Term Incentive Plans ('MTIP'), which run for three years. The expected cost under each plan is provided for when each grant is made
- (3) Other provisions arise in the normal course of business and are expected to crystallise in the foreseeable future

24. SUBORDINATED LIABILITIES

	The Bank & The Group			
	2006 Interest Rate	2006 £'000	2005 Interest Rate	2005 £'000
Primary Capital Floating Rate Stock, due to National Westminster Bank Plc				
£ 13,300,000 (note a)	5.403%	13,300	4.799%	13,300
US \$ 15,000,000 (note b)	5.479%	7,633	4.705%	8,714
£ 10,000,000 (note c)	5.820%	10,000	5.139%	10,000
		30,933		32,014

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

24. SUBORDINATED LIABILITIES (continued)

- (a) This stock, issued in 1987 to the National Westminster Bank Plc, has no final maturity, but all or part of it may be redeemed by Coutts & Co at any time, subject to the prior consent of the Financial Services Authority
- (b) This stock, issued in 1988 to the National Westminster Bank Plc, has no final maturity, but all or part of it may be redeemed by Coutts & Co at any time, subject to the prior consent of the Financial Services Authority
- (c) This stock, issued in 2002 to the National Westminster Bank Plc, has a final maturity date of December 2017

These primary loan stock capital issues by the Bank are unsecured and are subordinated to the claims of senior creditors. The primary loan capital is available to absorb losses but ranks ahead of other existing capital in the event of liquidation.

25 CALLED-UP SHARE CAPITAL

	2006 £'000	2005 £'000
Authorised, allotted, called-up and fully paid		
41,333,333 (2005 – 41,333,333) ordinary shares of £1 each	41,333	41,333

26. REVALUATION RESERVE

	The Bank & The Group 2006 £'000	2005 £'000
Revaluation reserve	26,982	26,982

The Group's freehold and leasehold property occupied for its own use was recorded at valuation on the basis of existing use value. The Group has elected to use this valuation as at 31 December 2003 as deemed cost for its opening IFRS balance sheet. The corresponding revaluation reserve in relation to the freehold and leasehold property is as shown above. This will be released when the property is sold in accordance with IAS 16 'Property, Plant and Equipment'.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS

The table below summarises the maturity analysis for the Group as at 31 December 2006

Remaining maturity	On demand £'000	Under 1 month £'000	1-3 months £'000	3-6 months £'000	6-12 months £'000	1-5 years £'000	Over 5 years £'000	Undated £'000	Total £'000
Assets									
Cash and balances at central banks	2,042	-	-	-	-	-	-	-	2,042
Items in the course of collection from other banks	10,017	-	-	-	-	-	-	-	10,017
Loans and advances to banks	2,148,969	4,965,673	789,653	254,063	107,471	321,248	-	-	8,587,077
Loans and advances to customers	3,004,058	699,120	173,478	71,055	54,625	403,421	46,069	-	4,451,826
Equity shares	-	-	-	-	-	-	-	12	12
Property, plant and equipment	-	-	133	5	694	4,216	65,522	-	70,570
Derivatives at fair value	-	512	721	587	-	170	1,495	-	3,485
Other assets, prepayments and accrued income	13,185	136,340	3,556	9,061	474	16,164	253	-	179,033
	<u>5,178,271</u>	<u>5,801,645</u>	<u>967,541</u>	<u>334,771</u>	<u>163,264</u>	<u>745,219</u>	<u>113,339</u>	<u>12</u>	<u>13,304,062</u>
Liabilities									
Deposits by banks	3,626	97,820	187,251	133,706	61,831	335,521	42,389	-	862,144
Items in the course of transmission to other banks	6,933	-	-	-	-	-	-	-	6,933
Customer accounts	7,631,940	3,077,237	717,309	93,468	28,163	109,842	-	-	11,657,959
Derivatives at fair value	-	589	132	-	915	169	253	-	2,058
Other liabilities, accruals and deferred income	41,278	241,304	22,368	-	-	-	-	-	304,950
Provisions for liabilities and charges	-	-	2,180	794	-	7,472	-	-	10,446
Subordinated liabilities	-	-	10,000	20,933	-	-	-	-	30,933
Shareholders' equity	-	-	-	-	-	-	-	428,639	428,639
	<u>7,683,777</u>	<u>3,416,950</u>	<u>939,240</u>	<u>248,901</u>	<u>90,909</u>	<u>453,004</u>	<u>42,642</u>	<u>428,639</u>	<u>13,304,062</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the maturity analysis for the Bank as at 31 December 2006

Remaining maturity	On demand £'000	Under 1 month £'000	1-3 months £'000	3-6 months £'000	6-12 months £'000	1-5 years £'000	Over 5 years £'000	Undated £'000	Total £'000
Assets									
Cash and balances at central banks	2,042	-	-	-	-	-	-	-	2,042
Items in the course of collection from other banks	10,017	-	-	-	-	-	-	-	10,017
Loans and advances to banks	2,148,969	4,965,673	789,653	254,063	107,471	321,248	-	-	8,587,077
Loans and advances to customers	3,001,924	1,157,571	151,528	49,084	10,656	24,485	36,186	-	4,431,434
Equity shares	-	-	-	-	-	-	-	12	12
Shares in group undertakings	-	-	-	-	-	-	-	3,350	3,350
Property, plant and equipment	-	-	133	5	694	4,216	65,522	-	70,570
Derivatives at fair value	-	512	721	587	-	170	1,495	-	3,485
Other assets, prepayments and accrued income	12,919	136,340	3,556	9,061	474	16,164	253	-	178,767
	<u>5,175,871</u>	<u>6,260,096</u>	<u>945,591</u>	<u>312,800</u>	<u>119,295</u>	<u>366,283</u>	<u>103,456</u>	<u>3,362</u>	<u>13,286,754</u>
Liabilities									
Deposits by banks	2,806	97,820	189,061	133,706	61,831	335,521	42,389	-	863,134
Items in the course of transmission to other banks	6,933	-	-	-	-	-	-	-	6,933
Customer accounts	7,633,612	3,077,237	717,309	93,468	28,163	109,842	-	-	11,659,631
Derivatives at fair value	-	589	132	-	915	169	253	-	2,058
Other liabilities, accruals and deferred income	38,744	241,179	22,369	-	-	-	-	-	302,292
Provisions for liabilities and charges	-	-	2,180	794	-	7,472	-	-	10,446
Subordinated liabilities	-	-	10,000	20,933	-	-	-	-	30,933
Shareholders' equity	-	-	-	-	-	-	-	411,327	411,327
	<u>7,682,095</u>	<u>3,416,825</u>	<u>941,051</u>	<u>248,901</u>	<u>90,909</u>	<u>453,004</u>	<u>42,642</u>	<u>411,327</u>	<u>13,286,754</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the maturity analysis for the Group as at 31 December 2005

Remaining maturity	On demand £'000	Under 1 month £'000	1-3 months £'000	3-6 months £'000	6-12 months £'000	1-5 years £'000	Over 5 years £'000	Undated £'000	Total £'000
Assets									
Cash and balances at central banks	1,776	-	-	-	-	-	-	-	1,776
Items in the course of collection from other banks	43,503	-	-	-	-	-	-	-	43,503
Loans and advances to banks	383,442	5,307,096	907,639	296,523	81,569	239,434	-	-	7,215,703
Loans and advances to customers	1,444,143	775,609	381,190	227,947	426,940	468,009	119,122	-	3,842,960
Equity shares	-	-	-	-	-	-	-	18	18
Intangible assets	-	-	-	1,210	-	-	-	-	1,210
Property, plant and equipment	-	-	36	1,244	705	3,646	64,999	-	70,630
Derivatives at fair value	-	1,117	-	-	-	293	3,328	-	4,738
Other assets, prepayments and accrued income	39,033	13,518	8,589	3,810	3,265	17,878	1,819	-	87,912
	<u>1,911,897</u>	<u>6,097,340</u>	<u>1,297,454</u>	<u>530,734</u>	<u>512,479</u>	<u>729,260</u>	<u>189,268</u>	<u>18</u>	<u>11,268,450</u>
Liabilities									
Deposits by banks	112,015	68,554	112,497	77,620	72,238	270,805	34,383	-	748,112
Items in the course of transmission to other banks	39,445	-	-	-	-	-	-	-	39,445
Customer accounts	6,159,748	2,932,336	607,973	98,122	36,130	95,797	10,406	-	9,940,512
Derivatives at fair value	-	1,084	-	-	-	293	3,328	-	4,705
Other liabilities, accruals and deferred income	134,269	3,223	6,122	3,246	16,448	8,640	-	-	171,948
Provisions for liabilities and charges	-	-	-	5,995	-	8,428	-	-	14,423
Subordinated liabilities	22,014	-	-	-	-	-	10,000	-	32,014
Shareholders' equity	-	-	-	-	-	-	-	317,291	317,291
	<u>6,467,491</u>	<u>3,005,197</u>	<u>726,592</u>	<u>184,983</u>	<u>124,816</u>	<u>383,963</u>	<u>58,117</u>	<u>317,291</u>	<u>11,268,450</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the maturity analysis for the Bank as at 31 December 2005

Remaining maturity	On demand £'000	Under 1 month £'000	1-3 months £'000	3-6 months £'000	6-12 months £'000	1-5 years £'000	Over 5 years £'000	Undated £'000	Total £'000
Assets									
Cash and balances at central banks	1,776	-	-	-	-	-	-	-	1,776
Items in the course of collection from other banks	43,503	-	-	-	-	-	-	-	43,503
Loans and advances to banks	383,442	5,312,096	907,639	296,523	81,569	239,434	-	-	7,220,703
Loans and advances to customers	1,423,754	775,609	381,190	227,947	426,940	468,009	119,122	-	3,822,571
Equity shares	-	-	-	-	-	-	-	18	18
Shares in group undertakings	-	-	-	-	-	-	-	3,350	3,350
Intangible assets	-	-	-	1,210	-	-	-	-	1,210
Property, plant and equipment	-	-	36	1,244	705	3,646	64,999	-	70,630
Derivatives at fair value	-	1,117	-	-	-	293	3,328	-	4,738
Other assets, prepayments and accrued income	41,385	13,512	8,311	3,791	3,229	17,544	2,493	-	90,265
	<u>1,893,860</u>	<u>6,102,334</u>	<u>1,297,176</u>	<u>530,715</u>	<u>512,443</u>	<u>728,926</u>	<u>189,942</u>	<u>3,368</u>	<u>11,258,764</u>
Liabilities									
Deposits by banks	112,015	68,554	112,497	77,620	72,238	270,805	34,383	-	748,112
Items in the course of transmission to other banks	39,445	-	-	-	-	-	-	-	39,445
Customer accounts	6,160,268	2,932,336	606,476	96,728	38,249	86,862	20,113	-	9,941,032
Derivatives at fair value	-	1,084	-	-	-	293	3,328	-	4,705
Other liabilities, accruals and deferred income	135,466	3,223	6,122	3,246	16,448	8,640	-	-	173,145
Provisions for liabilities and charges	-	-	-	5,995	-	8,428	-	-	14,423
Subordinated liabilities	22,014	-	-	-	-	-	10,000	-	32,014
Shareholders' equity	-	-	-	-	-	-	-	305,888	305,888
	<u>6,469,208</u>	<u>3,005,197</u>	<u>725,095</u>	<u>183,589</u>	<u>126,935</u>	<u>375,028</u>	<u>67,824</u>	<u>305,888</u>	<u>11,258,764</u>

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the interest rate sensitivity gaps for the Group at 31 December 2006

	On demand or short notice	3 months or less	After 3 months but less than 6 months	After 6 months but less than 1 year	After 1 year but less than 5 years	Over 5 years	Non interest earning /bearing	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Assets								
Cash and balances at central banks	2,042	-	-	-	-	-	-	2,042
Items in the course of collection from other banks	10,017	-	-	-	-	-	-	10,017
Loans and advances to banks	2,022,050	5,616,816	228,435	102,642	225,025	-	392,109	8,587,077
Loans and advances to customers	3,008,454	872,598	71,054	54,625	403,421	28,349	13,325	4,451,826
Derivatives at fair value	-	-	-	-	-	-	3,485	3,485
Other assets	-	-	-	-	-	-	249,615	249,615
Total assets	5,042,563	6,489,414	299,489	157,267	628,446	28,349	658,534	13,304,062
Liabilities and equity								
Deposits by banks	8,959	279,738	133,706	61,831	335,521	42,389	-	862,144
Items in the course of transmission to other banks	6,933	-	-	-	-	-	-	6,933
Customer accounts	7,605,086	3,792,960	93,468	28,164	109,843	-	28,438	11,657,959
Derivatives at fair value	-	-	-	-	-	-	2,058	2,058
Other liabilities	-	-	-	-	-	-	315,396	315,396
Subordinated liabilities	-	10,000	20,933	-	-	-	-	30,933
Shareholders' equity	-	-	-	-	-	-	428,639	428,639
Total liabilities and equity	7,620,978	4,082,698	248,107	89,995	445,364	42,389	774,531	13,304,062
Off Balance Sheet Items (see below)	-	(315,330)	-	315,330	-	-	-	-
Interest rate sensitivity gap	(2,578,415)	2,091,386	51,382	382,602	183,082	(14,040)	(115,997)	-
Cumulative interest rate sensitivity gap	(2,578,415)	(487,029)	(435,647)	(53,045)	130,037	115,997	-	-

The carrying amounts of derivative assets and liabilities represent fair values and have thus been included under the heading of non-interest bearing. Interest rate risk on these instruments has been reflected through the off-balance sheet gap which represents the notional principal amounts in respect of interest rate derivatives utilised for both trading and in managing the interest rate risk position of the Group.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the interest rate sensitivity gaps for the Bank at 31 December 2006

	On demand or short notice	3 months or less	After 3 months but less than 6 months	After 6 months but less than 1 year	After 1 year but less than 5 years	Over 5 years	Non interest earning /bearing	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Assets								
Cash and balances at central banks	2,042	-	-	-	-	-	-	2,042
Items in the course of collection from other banks	10,017	-	-	-	-	-	-	10,017
Loans and advances to banks	2,022,050	5,616,816	228,435	102,642	225,025	-	392,109	8,587,077
Loans and advances to customers	3,008,454	852,206	71,054	54,625	403,421	28,349	13,325	4,431,434
Derivatives at fair value	-	-	-	-	-	-	3,485	3,485
Other assets	-	-	-	-	-	-	252,699	252,699
Total assets	5,042,563	6,469,022	299,489	157,267	628,446	28,349	661,618	13,286,754
Liabilities and equity								
Deposits by banks	8,139	281,548	133,706	61,831	335,521	42,389	-	863,134
Items in the course of transmission to other banks	6,933	-	-	-	-	-	-	6,933
Customer accounts	7,605,906	3,793,812	93,468	28,164	109,843	-	28,438	11,659,631
Derivatives at fair value	-	-	-	-	-	-	2,058	2,058
Other liabilities	-	-	-	-	-	-	312,738	312,738
Subordinated liabilities	-	10,000	20,933	-	-	-	-	30,933
Shareholders' equity	-	-	-	-	-	-	411,327	411,327
Total liabilities and equity	7,620,978	4,085,360	248,107	89,995	445,364	42,389	754,561	13,286,754
Off Balance Sheet Items (see below)	-	(315,330)	-	315,330	-	-	-	-
Interest rate sensitivity gap	(2,578,415)	2,068,332	51,382	382,602	183,082	(14,040)	(92,943)	-
Cumulative interest rate sensitivity gap	(2,578,415)	(510,083)	(458,701)	(76,099)	106,983	92,943	-	-

The carrying amounts of derivative assets and liabilities represent fair values and have thus been included under the heading of non-interest bearing. Interest rate risk on these instruments has been reflected through the off-balance sheet gap which represents the notional principal amounts in respect of interest rate derivatives utilised for both trading and in managing the interest rate risk position of the Bank.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the interest rate sensitivity gaps for the Group at 31 December 2005

	On demand or short notice	3 months or less	After 3 months but less than 6 months	After 6 months but less than 1 year	After 1 year but less than 5 years	Over 5 years	Non interest earning /bearing	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Assets								
Cash and balances at central banks	1,776	-	-	-	-	-	-	1,776
Items in the course of collection from other banks	43,503	-	-	-	-	-	-	43,503
Loans and advances to banks	275,149	5,265,565	893,897	256,519	60,114	140,460	323,999	7,215,703
Loans and advances to customers	1,444,143	1,156,799	227,947	426,940	468,009	119,122	-	3,842,960
Derivatives at fair value	-	-	-	-	-	-	4,738	4,738
Other assets	-	-	-	-	-	-	159,770	159,770
Total assets	1,764,571	6,422,364	1,121,844	683,459	528,123	259,582	488,507	11,268,450
Liabilities and equity								
Deposits by banks	111,268	177,691	76,020	69,703	261,525	34,383	17,522	748,112
Items in the course of transmission to other banks	39,445	-	-	-	-	-	-	39,445
Customer accounts	6,140,509	3,540,309	98,122	36,130	95,797	10,406	19,239	9,940,512
Derivatives at fair value	-	-	-	-	-	-	4,705	4,705
Other liabilities	-	-	-	-	-	-	186,371	186,371
Subordinated liabilities	-	10,000	22,014	-	-	-	-	32,014
Shareholders' equity	-	-	-	-	-	-	317,291	317,291
Total liabilities and equity	6,291,222	3,728,000	196,156	105,833	357,322	44,789	545,128	11,268,450
Off balance sheet items	-	(1,111,409)	-	1,111,409	-	-	-	-
Interest rate sensitivity gap	(4,526,651)	1,582,955	925,688	1,689,035	170,801	214,793	(56,621)	-
Cumulative interest rate sensitivity gap	(4,526,651)	(2,943,696)	(2,018,008)	(328,973)	(158,172)	56,621	-	-

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the interest rate sensitivity gaps for the Bank at 31 December 2005

	On demand or short notice	3 months or less	After 3 months but less than 6 months	After 6 months but less than 1 year	After 1 year but less than 5 years	Over 5 years	Non interest earning /bearing	Total
	£'000	£'000	£'000	£'000	£'000	£'000	£'000	£'000
Assets								
Cash and balances at central banks	1,776	-	-	-	-	-	-	1,776
Items in the course of collection from other banks	43,503	-	-	-	-	-	-	43,503
Loans and advances to banks	275,149	5,270,565	893,897	256,519	60,114	140,460	323,999	7,220,703
Loans and advances to customers	1,423,754	1,156,799	227,947	426,940	468,009	119,122	-	3,822,571
Derivatives at fair value	-	-	-	-	-	-	4,738	4,738
Other assets	-	-	-	-	-	-	165,473	165,473
Total assets	1,744,182	6,427,364	1,121,844	683,459	528,123	259,582	494,210	11,258,764
Liabilities and equity								
Deposits by banks	111,268	177,691	76,020	69,703	261,525	34,383	17,522	748,112
Items in the course of transmission to other banks	39,445	-	-	-	-	-	-	39,445
Customer accounts	6,141,029	3,540,309	98,122	36,130	95,797	10,406	19,239	9,941,032
Derivatives at fair value	-	-	-	-	-	-	4,705	4,705
Other liabilities	-	-	-	-	-	-	187,568	187,568
Subordinated liabilities	-	10,000	22,014	-	-	-	-	32,014
Shareholders' equity	-	-	-	-	-	-	305,888	305,888
Total liabilities and equity	6,291,742	3,728,000	196,156	105,833	357,322	44,789	534,922	11,258,764
Off balance sheet items	-	(1,111,409)	-	1,111,409	-	-	-	-
Interest rate sensitivity gap	(4,547,560)	1,587,955	925,688	1,689,035	170,801	214,793	(40,712)	
Cumulative interest rate sensitivity gap	(4,547,560)	(2,959,605)	(2,033,917)	(344,882)	(174,081)	40,712	-	

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The following table shows the carrying values and where different the fair values of financial instruments on the Group's balance sheet

	2006		2005	
	Carrying value £'000	Fair value £'000	Carrying value £'000	Fair value £'000
Financial assets				
Cash and balances at central banks	2,042	2,042	1,776	1,776
Items in course of collection	10,017	10,017	43,503	43,503
Loans and advances to banks				
Loans and receivables	8,587,077	8,587,077	7,215,703	7,215,703
Loans and advances to customers				
Loans and receivables	4,451,826	4,451,826	3,842,960	3,842,960
Derivatives at fair value	3,485	3,485	4,738	4,738
Financial liabilities				
Deposits by banks				
Amortised cost	862,144	862,144	748,112	748,112
Items in the course of transmission	6,933	6,933	39,445	39,445
Customer accounts				
Amortised cost	11,657,959	11,657,959	9,940,512	9,940,512
Subordinated debt				
Amortised cost	30,933	30,933	32,014	32,014
Derivatives at fair value	2,058	2,058	4,705	4,705

NOTES TO THE ACCOUNTS (continued)**Year ended 31 December 2006****27. FINANCIAL INSTRUMENTS (continued)**

The following table shows the carrying values and where different the fair values of financial instruments on the Bank's balance sheet

	2006		2005	
	Carrying value £'000	Fair value £'000	Carrying value £'000	Fair value £'000
Financial assets				
Cash and balances at central banks	2,042	2,042	1,776	1,776
Items in course of collection	10,017	10,017	43,503	43,503
Loans and advances to banks				
Loans and receivables	8,587,077	8,587,077	7,220,703	7,220,703
Loans and advances to customers				
Loans and receivables	4,431,434	4,431,434	3,822,571	3,822,571
Derivatives at fair value	3,485	3,485	4,738	4,738
Financial liabilities				
Deposits by banks				
Amortised cost	863,134	863,134	748,112	748,112
Items in the course of transmission	6,933	6,933	39,445	39,445
Customer accounts				
Amortised cost	11,659,631	11,659,631	9,941,032	9,941,032
Subordinated debt				
Amortised cost	30,933	30,933	32,014	32,014
Derivatives at fair value	2,058	2,058	4,705	4,705

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the assets and liabilities of the Group denominated in Sterling and Foreign Currency as at 31 December 2006

	Sterling £'000	US Dollars £'000	Euro £'000	Other £'000	Total £'000
Assets					
Cash and balances at central banks	2,042	-	-	-	2,042
Items in the course of collection from other banks	9,303	278	383	53	10,017
Loans and advances to banks	7,302,979	952,677	272,862	58,559	8,587,077
Loans and advances to customers	4,128,757	115,810	107,193	100,066	4,451,826
Equity shares	12	-	-	-	12
Property, plant and equipment	70,570	-	-	-	70,570
Derivatives at fair value	1,830	1,652	(4)	7	3,485
Other assets, prepayments and accrued income	165,374	10,862	2,398	399	179,033
Total assets	11,680,867	1,081,279	382,832	159,084	13,304,062
Liabilities and equity					
Deposits by banks	763,128	13,894	14,892	70,230	862,144
Items in the course of transmission to other banks	6,933	-	-	-	6,933
Customer accounts	10,199,354	1,019,988	350,290	88,327	11,657,959
Derivatives at fair value	2,058	-	-	-	2,058
Other liabilities, accruals and deferred income	304,936	5	9	-	304,950
Provisions for liabilities and charges	10,446	-	-	-	10,446
Subordinated liabilities	23,300	7,633	-	-	30,933
Shareholders' equity	418,977	6,822	2,077	763	428,639
Total liabilities and equity	11,729,132	1,048,342	367,268	159,320	13,304,062

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the assets and liabilities of the Bank denominated in Sterling and Foreign Currency as at 31 December 2006

	Sterling £'000	US Dollars £'000	Euro £'000	Other £'000	Total £'000
Assets					
Cash and balances at central banks	2,042	-	-	-	2,042
Items in the course of collection from other banks	9,303	278	383	53	10,017
Loans and advances to banks	7,302,979	952,677	272,862	58,559	8,587,077
Loans and advances to customers	4,108,365	115,810	107,193	100,066	4,431,434
Equity shares	12	-	-	-	12
Shares in group undertakings	3,350	-	-	-	3,350
Property, plant and equipment	70,570	-	-	-	70,570
Derivatives at fair value	1,830	1,652	(4)	7	3,485
Other assets, prepayments and accrued income	165,108	10,862	2,398	399	178,767
Total assets	11,663,559	1,081,279	382,832	159,084	13,286,754
Liabilities and equity					
Deposits by banks	740,408	24,748	26,863	71,115	863,134
Items in the course of transmission to other banks	6,933	-	-	-	6,933
Customer accounts	10,201,026	1,019,988	350,290	88,327	11,659,631
Derivatives at fair value	2,058	-	-	-	2,058
Other liabilities, accruals and deferred income	302,278	5	9	-	302,292
Provisions for liabilities and charges	10,446	-	-	-	10,446
Subordinated liabilities	23,300	7,633	-	-	30,933
Shareholders' equity	401,665	6,822	2,077	763	411,327
Total liabilities and equity	11,688,114	1,059,196	379,239	160,205	13,286,754

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the assets and liabilities of the Group denominated in Sterling and Foreign Currency as at 31 December 2005

	Sterling £'000	US Dollars £'000	Euro £'000	Other £'000	Total £'000
Assets					
Cash and balances at central banks	1,776	-	-	-	1,776
Items in the course of collection from other banks	42,876	480	146	1	43,503
Loans and advances to banks	6,277,009	705,829	217,990	14,875	7,215,703
Loans and advances to customers	3,552,570	142,707	78,124	69,559	3,842,960
Equity shares	18	-	-	-	18
Intangible assets	1,210	-	-	-	1,210
Property, plant and equipment	70,630	-	-	-	70,630
Derivatives at fair value	4,738	-	-	-	4,738
Other assets, prepayments and accrued income	76,310	9,525	1,756	321	87,912
Total assets	10,027,137	858,541	298,016	84,756	11,268,450
Liabilities and equity					
Deposits by banks	638,313	52,649	41,893	15,257	748,112
Items in the course of transmission to other banks	39,445	-	-	-	39,445
Customer accounts	8,862,023	768,519	246,239	63,731	9,940,512
Derivatives at fair value	4,705	-	-	-	4,705
Other liabilities, accruals and deferred income	171,480	260	133	75	171,948
Provisions for liabilities and charges	14,423	-	-	-	14,423
Subordinated liabilities	23,300	8,714	-	-	32,014
Shareholders' equity	293,038	16,599	5,747	1,907	317,291
Total liabilities and equity	10,046,727	846,741	294,012	80,970	11,268,450

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the assets and liabilities of the Bank denominated in Sterling and Foreign Currency as at 31 December 2005

	Sterling £'000	US Dollars £'000	Euro £'000	Other £'000	Total £'000
Assets					
Cash and balances at central banks	1,776	-	-	-	1,776
Items in the course of collection from other banks	42,876	480	146	1	43,503
Loans and advances to banks	6,282,009	705,829	217,990	14,875	7,220,703
Loans and advances to customers	3,532,181	142,707	78,124	69,559	3,822,571
Equity shares	18	-	-	-	18
Shares in group undertakings	3,350	-	-	-	3,350
Intangible assets	1,210	-	-	-	1,210
Property, plant and equipment	70,630	-	-	-	70,630
Derivatives at fair value	4,738	-	-	-	4,738
Other assets, prepayments and accrued income	78,663	9,525	1,756	321	90,265
Total assets	10,017,451	858,541	298,016	84,756	11,258,764
Liabilities and equity					
Deposits by banks	638,313	52,649	41,893	15,257	748,112
Items in the course of transmission to other banks	39,445	-	-	-	39,445
Customer accounts	8,862,543	768,519	246,239	63,731	9,941,032
Derivatives at fair value	4,705	-	-	-	4,705
Other liabilities, accruals and deferred income	172,677	260	133	75	173,145
Provisions for liabilities and charges	14,423	-	-	-	14,423
Subordinated liabilities	23,300	8,714	-	-	32,014
Shareholders' equity	288,991	12,988	2,846	1,063	305,888
Total liabilities and equity	10,044,397	843,130	291,111	80,126	11,258,764

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the segmental industrial classification for the Group

	2006		2005	
	Loans and advances to banks £'000	Loans and advances to customers £'000	Loans and advances to banks £'000	Loans and advances to customers £'000
Central and local government	-	645	-	709
Manufacturing	-	6,908	-	10,316
Construction	-	495	-	654
Finance	8,589,041	268,108	7,193,834	222,774
Service industry and business activities	-	141,879	-	149,456
Agriculture, forestry and fishing	-	7,774	-	8,772
Property	-	434,922	-	356,817
Other business activities	-	112,281	-	80,727
Individuals				
Home mortgages	-	1,760,548	-	1,555,457
Other	-	1,720,413	-	1,462,041
Lease financing	-	-	-	15
Interest accruals	-	15,575	23,833	14,213
Total	8,589,041	4,469,548	7,217,667	3,861,951
Provisions and impairment (note 14)	(1,964)	(17,722)	(1,964)	(18,991)
Total	8,587,077	4,451,826	7,215,703	3,842,960

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the segmental industrial classification for the Bank.

	2006		2005	
	Loans and advances to banks £'000	Loans and advances to customers £'000	Loans and advances to banks £'000	Loans and advances to customers £'000
Central and local government	-	645	-	709
Manufacturing	-	6,908	-	10,316
Construction	-	495	-	654
Finance	8,589,041	268,108	7,198,834	222,774
Service industry and business activities	-	141,879	-	149,456
Agriculture, forestry and fishing	-	7,774	-	8,772
Property	-	434,922	-	356,817
Other business activities	-	112,281	-	60,281
Individuals				
Home mortgages	-	1,742,290	-	1,555,457
Other	-	1,720,413	-	1,462,041
Lease financing	-	-	-	15
Interest accruals	-	13,441	23,833	14,213
Total	8,589,041	4,449,156	7,222,667	3,841,505
Provisions and impairment (note 14)	(1,964)	(17,722)	(1,964)	(18,934)
Total	8,587,077	4,431,434	7,220,703	3,822,571

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

Risk Management

The major risks faced by the Group are market risk, liquidity risk, credit risk and operational risk. The Group has established a comprehensive framework for managing these risks which is continually evolving as the Group's business activities change in response to market, credit, product and other developments

Market risk

Market risk is the risk that changes in interest rates, foreign exchange rates, prices, volatilities and correlations, may have an adverse financial impact on the Group's financial condition or results

The Group does not maintain any material proprietary trading positions and consequently has limited exposure to market risk. The market risk that arises through the provision of products and services to customers, being principally interest rate and foreign exchange risk, is predominantly hedged. Unhedged market risk is small in accordance with policy limits.

Interest rate risk arises where assets and liabilities of the Group have different repricing dates. Group policy requires all interest rate risk to be transferred to trading units either within the RBS Group or with third parties, through arm's length cash transactions and derivatives, principally through interest rate swaps and loans with RBS Group.

The Group does not maintain material open currency positions. The Group has no structural foreign currency exposures as all investments in subsidiaries are denominated in sterling.

Value-at-risk (VaR)

The Group manages the market risk in its treasury portfolios through value-at-risk (VaR) limits as well as stress testing, position and sensitivity limits. VaR is a technique that produces estimates of the potential negative change in the market value of a portfolio over a specified time horizon at a given confidence level.

Liquidity risk

The management of the Group's liquidity aims to ensure that the Group can meet deposit withdrawals either on demand or at contractual maturity, to meet customer demands for new loans and to repay borrowings as they mature. Diversification of sources of deposits and borrowings and management of maturities are used to ensure ready access to funds at all times. The Group's liquidity management meets the requirements of the FSA.

Credit risk

Credit risk is the risk that companies, financial institutions, individuals and other counterparties may be unable to meet their obligations to the Group. Credit risk arises principally from the Group's lending activities and is monitored by the Credit risk department who analyse lending into segments by internal risk classification and by type of loan. For any exposures that are individually assessed a specific provision is made against the loan with regard to the specific financial circumstances of the counterparty.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This risk is managed through systems and procedures to monitor transactions, and the documentation of transactions and periodic review by internal audit.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

27. FINANCIAL INSTRUMENTS (continued)

The table below summarises the off-balance sheet instruments for the Group at 31 December 2006

	Notional principal amount £000	2006 Fair value		2006 Carrying value	
		Asset £000	Liability £000	Asset £000	Liability £000
Exchange rate related contracts					
Forward foreign exchange	124,098	1,821	1,738	1,821	1,738
Of which third party	68,841	983	1,017	983	1,017
Interest rate related contracts					
Futures, forwards and options	191,232	1,664	320	1,664	320
Of which third party	95,616	1,664	320	1,664	320

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 liquidation or sale

The fair value of derivatives held for non-trading purposes is determined by market prices, or, where market prices are not available, by applying current market information to pricing or valuation models

The fair value of all other financial assets and liabilities at the balance sheet date has not been disclosed due to no active market existing for these assets and liabilities

The table below summarises the off-balance sheet instruments for the Group at 31 December 2005

	Notional principal amount £000	2005 Fair value		2005 Carrying value	
		Asset £000	Liability £000	Asset £000	Liability £000
Exchange rate related contracts					
Forward foreign exchange	185,257	1,117	1,075	1,117	1,075
Of which third party	94,231	1,117	630	1,117	630
Interest rate related contracts					
Interest rate swaps	801,000	-	9	-	9
Futures, forwards and options	125,152	3,621	3,621	3,621	3,621
Of which third party	62,576	3,621	3,621	3,621	3,621

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

28 MEMORANDUM ITEMS

The following tables give, for the Bank and Group, the nominal principal amounts and risk weighted amounts for certain off-balance sheet transactions. The nominal principal amounts indicate the volume of business outstanding at the balance sheet date and do not represent amounts at risk. The risk weighted amounts have been calculated in accordance with the Financial Services Authority ('FSA') guidelines implementing the Basel agreement on capital adequacy.

Memorandum Items

	2006		2005	
	Contract amount £'000	Risk weighted amount £'000	Contract amount £'000	Risk weighted amount £'000
The Bank and the Group				
Contingent liabilities				
Acceptances and endorsements	122	122	30	30
Guarantees and assets pledged as collateral security				
Guarantees and irrevocable letters of credit	157,825	140,272	122,749	96,836
Other contingent liabilities	3,380	1,690	3,226	1,613
Total contingent liabilities	161,327	142,084	126,005	98,479
The Group				
Commitments				
Documentary credits and other short-term trade-related contingencies	395	-	247	-
Undrawn formal standby facilities, credit lines and other commitments to lend				
1 year and over	40,625	20,313	28,448	14,224
Less than 1 year	2,265,923	-	2,019,306	-
Total commitments	2,306,943	20,313	2,048,001	14,224
The Bank				
Commitments				
Documentary credits and other short-term trade-related contingencies	395	-	247	-
Undrawn formal standby facilities, credit lines and other commitments to lend				
1 year and over	40,625	20,313	28,436	14,218
Less than 1 year	2,087,735	-	1,865,967	-
Total commitments	2,128,755	20,313	1,894,650	14,218

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

28. MEMORANDUM ITEMS (continued)

	The Bank and The Group	
	2006	2005
	£'000	£'000
(i) Operating lease commitments		
At the year end, annual commitments under non-cancellable operating leases were		
Premises - operating leases which expire		
- within one year	142	119
- between one and five years	1,704	1,689
- in five years or more	2,075	1,943

- (i) The commitments under non-cancellable operating leases are paid annually as part of Coutts management recharge to The Royal Bank of Scotland Group plc (note 34)
- (ii) Management and agency services The Group provides investment management services Funds under management at 31 December 2006 were £7,345m (2005 - £5,973m)
- (iii) Future contracted capital expenditure The Group has contracted capital expenditure not provided for in the accounts of £13,880,000 (2005 - £15,600,000)

Contingent liabilities

Acceptances – in accepting a bill of exchange drawn on it by a customer a bank undertakes to pay the holder of the bill at maturity Most acceptances are presented for payment and reimbursement by the customer is usually immediate In the UK, bills accepted by certain banks designated by the Bank of England are eligible for rediscount at the Bank of England

Endorsements – in endorsing a bill of exchange a bank accepts liability for payment of any shortfall on the bill at maturity Unlike acceptances, the endorsing bank receives value for the bill, which is then rediscounted

Guarantees – the Group gives guarantees on behalf of customers A financial guarantee represents an irrevocable undertaking that the Group will meet a customer's obligations to third parties if the customer fails to do so The maximum amount that the Group could be required to pay under a guarantee is its principal amount as disclosed in the table above The Group expects most guarantees it provides to expire unused

Other contingent liabilities – these include standby letters of credit, supporting customer debt issues and contingent liabilities relating to customer trading activities such as those arising from performance and customs bonds, warranties and indemnities

Commitments

Banking commitments and contingent obligations, which have been entered into on behalf of customers and for which there are corresponding obligations from customers, are not included in assets and liabilities The Group's maximum exposure to credit loss, in the event of non-performance by the other party and where all counterclaims, collateral or security proves valueless, is represented by the contractual nominal amount of these instruments included in the table These commitments and contingent obligations are subject to the Group's normal credit approval processes and any potential loss is taken into account in assessing provisions for bad and doubtful debts in accordance with the Group's provisioning policy

Commitments to lend – under a loan commitment the Group agrees to make funds available to a customer in the future Loan commitments, which are usually for a specified term may be unconditionally cancellable or may persist, provided all conditions in the loan facility are satisfied or waived Commitments to lend include commercial standby facilities and credit lines, liquidity facilities to commercial paper conduits and unutilised overdraft facilities

Other commitments – these include forward asset purchases, forward deposits placed and undrawn note issuance and revolving underwriting facilities

NOTES TO THE ACCOUNTS (continued)**Year ended 31 December 2006****28. MEMORANDUM ITEMS (continued)**

Additional contingent liabilities arise in the normal course of the Group's business. It is not anticipated that any material loss will arise from these transactions.

Litigation

The Group is involved in litigation involving claims by and against it which arise in the ordinary course of business. The directors of the Group have reviewed these actual, threatened and known potential claims and proceedings and, after consulting with the relevant legal advisers are satisfied that the outcome of these claims and proceedings will not have a material adverse effect on the Group's consolidated net assets, results of operations or cash flows.

29. NET CASH INFLOW FROM OPERATING ACTIVITIES

	The Bank		The Group	
	2006	2005	2006	2005
	£'000	£'000	£'000	£'000
Operating profit	155,325	99,320	163,768	107,840
Provisions for bad and doubtful debts	408	4,228	408	5,183
Loans and advances written off net of recoveries	(1,677)	1,821	(1,677)	1,821
Loss on sale of tangible fixed assets	(1)	(8)	(1)	(8)
Provisions for liabilities and charges	-	600	-	600
Provisions utilised	(3,977)	(4,827)	(3,977)	(4,827)
Depreciation and amortisation of tangible and intangible assets	6,101	11,423	6,101	11,423
Net cash inflow from trading activities	854	13,237	854	14,192
Decrease/(increase) in items in the course of collection	33,486	(19,442)	33,486	(19,442)
Increase/(decrease) in loans and advances to banks	399,153	(558,182)	394,153	(558,182)
Increase in loans and advances to customers	(607,651)	(596,058)	(607,597)	(595,967)
(Increase)/decrease in other assets, prepayments and accrued income	(92,831)	43,955	(92,843)	38,980
Changes in operating assets	(267,843)	(1,129,727)	(272,801)	(1,134,611)
(Decrease)/increase in items in the course of transmission	(32,512)	37,291	(32,512)	37,291
Increase in deposits by banks	115,022	172,778	114,032	172,778
Increase in customer accounts	1,718,599	1,091,823	1,717,447	1,091,890
Increase/(decrease) in other liabilities, accruals and deferred income	124,880	(38,293)	126,198	(39,282)
Effect of other accruals/deferrals and other non-cash movements	(2,575)	(1,502)	(2,633)	(2,298)
Changes in operating liabilities	1,923,414	1,262,097	1,922,532	1,260,379
Total income taxes paid	(41,126)	(32,217)	(43,729)	(35,090)
Net cash inflow from operating activities	1,770,624	212,710	1,770,624	212,710

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

30. ANALYSIS OF CHANGES IN FINANCING DURING THE YEAR

	The Bank and The Group	
	2006	2005
	£'000	£'000
Loan Capital		
At 1 January	32,014	31,054
Currency translation	(1,081)	960
At 31 December	<u>30,933</u>	<u>32,014</u>

31. ANALYSIS OF CASH AND CASH EQUIVALENTS

	The Bank and The Group	
	2006	2005
	£'000	£'000
At 1 January	385,218	192,008
Net cash inflow	<u>1,765,793</u>	<u>193,210</u>
At 31 December	<u>2,151,011</u>	<u>385,218</u>
Comprising		
Cash and balances at central banks	2,042	1,776
Loans and advances to banks repayable on demand	<u>2,148,969</u>	<u>383,442</u>
At 31 December	<u>2,151,011</u>	<u>385,218</u>

32. SEGMENTAL INFORMATION

The Group operates in the private banking sector, with 99% of business derived in the United Kingdom, and 1% of business derived in Monaco

The Directors consider private banking a single class of business

33. DIRECTORS' REMUNERATION

	2006	2005
	£'000	£'000
The remuneration of the directors of the Bank was as follows		
Emoluments	1,051	570
Pension contributions	1	2
Other	3	-
Total emoluments received by directors	<u>1,055</u>	<u>572</u>
Number of directors to whom retirement benefits are accruing in respect of qualifying services		
- money purchase schemes	2	1
- defined benefit schemes	3	2

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

33. DIRECTORS' REMUNERATION (continued)

The executive directors may also participate in the Company's executive share option and sharesave schemes and details of their interests in the Company's shares arising from their participation are contained on page 3

The total emoluments of the highest paid director were £350,228 (2005 – £291,285) The accrued pension attributable to that director was £17,351 (2005 – £37,952) No shares were received or receivable in respect of qualifying services under long-term incentive schemes

34. RELATED PARTY TRANSACTIONS

The aggregate amounts outstanding from directors, including connected persons, or officers of the Bank during the year, and the number of persons concerned were as follows

	Aggregate amount outstanding £'000	Number of persons
Directors		
Loans	126	5
Officers		
Loans	1,155	14

All of the above balances are classified under Loans and Advances to Customers

The captions in the primary financial statements include the following amounts attributable, in aggregate, to subsidiaries

	Advances	2006 Deposits	Closing Balance	Advances	2005 Deposits	Closing Balance
	£'000	£'000	£'000	£'000	£'000	£'000
Loans and advances to banks	-	-	-	-	-	5,000
Loans and advances to customers	104,147	-	1,049,291	53,364	-	945,144
Customer accounts	460	(1,611)	(1,672)	267	(201)	(521)
Other liabilities, accruals and deferred income	27,857	(28,851)	(1,810)	25,335	(26,151)	(816)
Interest receivable	-	-	-	-	(45,579)	(45,579)
Interest payable	1	-	1	2	-	2
Fees and commissions receivable	-	(62)	(62)	-	(527)	(527)

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

34. RELATED PARTY TRANSACTIONS (continued)

The captions in the primary financial statements include the following amounts attributable, in aggregate, to parent companies

	2006			2005		
	Advances	Deposits	Closing Balance	Advances	Deposits	Closing Balance
	£'000	£'000	£'000	£'000	£'000	£'000
Loans and advances to banks	6,489,789	(5,116,886)	8,573,718	764,880	(13,749)	7,200,815
Other assets, prepayments and accrued income	85,806	(1,674)	125,086	27,122	(57,604)	40,954
Deposits by banks	203,262	(310,888)	(833,080)	114,109	(293,275)	(725,454)
Other liabilities, accruals and deferred income	180,373	(295,778)	(246,862)	51,442	(33,897)	(131,457)
Subordinated liabilities	1,081	-	(30,933)	-	(960)	(32,014)
Interest receivable	-	(350,991)	(350,991)	-	(251,178)	(251,178)
Interest payable	34,349	-	34,349	24,227	-	24,227
Fees and commissions receivable	-	(42,143)	(42,143)	-	(28,753)	(28,753)
Fees and commissions payable	2,834	-	2,834	2,544	-	2,544

The captions in the primary financial statements include the following amounts attributable, in aggregate, to other related parties

	2006			2005		
	Advances	Deposits	Closing Balance	Advances	Deposits	Closing Balance
	£'000	£'000	£'000	£'000	£'000	£'000
Other assets, prepayments and accrued income	14,851	(8,682)	17,087	1,061	(3,394)	10,918
Deposits by banks	19,543	(23,539)	(20,105)	57,160	(45,161)	(16,109)
Other liabilities, accruals and deferred income	620	(786)	(892)	7,953	(3,593)	(726)
Interest payable	1,088	-	1,088	4,499	-	4,449
Fees and commissions receivable	-	(1,282)	(1,282)	-	(1,070)	(1,070)
Fees and commissions payable	377	-	377	271	-	271

None of the amounts due from related parties were impaired

Other operating charges represents a management recharge of £32,817,000 (2005 - £43,616,000) from The Royal Bank of Scotland Group plc

Share-based payments

Employee costs recharged by The Royal Bank of Scotland Group plc employer companies includes the full costs of key managers and other staff in respect of share-based payments. The attribution among members of The Royal Bank of Scotland Group plc has regard to the needs of the group as a whole. It would be inappropriate to deem that any employees had received share-based payments as a result of their employment with this Company.

NOTES TO THE ACCOUNTS (continued)
Year ended 31 December 2006

35. ULTIMATE PARENT COMPANY

The Bank's ultimate holding company, ultimate controlling party and the parent of the largest group in which the Bank's results are consolidated is The Royal Bank of Scotland Group plc which is incorporated in Great Britain and registered in Scotland. Copies of financial statements for The Royal Bank of Scotland Group plc, can be obtained from The Royal Bank of Scotland Group plc, Gogarburn, Edinburgh EH12 1HQ.

The immediate parent of the Company, which is also the smallest group into which the Company is consolidated, is National Westminster Bank Plc, a company incorporated in Great Britain and registered in England and Wales. Copies of the consolidated financial statements for this subgroup can be obtained from National Westminster Bank Plc, 135 Bishopsgate, London EC2M 3UR.

36. EVENTS AFTER THE BALANCE SHEET DATE

There have been no significant events between the year end and the date of approval of the accounts which would require a change or additional disclosure in the accounts.