Tesco Personal Finance plc

Basel II Pillar 3 Disclosures
28th February 2013

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1. Overview

1.1. Background

The European Union Capital Requirements Directive (Basel II) came into force on 1st January 2007, replacing the original Basel Accord (Basel I) agreed in 1988 by the Basel Committee on Banking Supervision. Implementation of Basel II in the UK has been achieved through a series of rules introduced by the UK's Regulatory Authorities. The Basel II framework consists of three "pillars":

Pillar 1 - sets out the minimum capital requirements firms are required to meet for credit, market and operational risk.

Pillar 2 - requires firms and supervisors to take a view on whether a firm should hold additional capital against risks considered under Pillar 1 that are not fully captured by the Pillar 1 process (e.g. credit concentration risk); those factors not taken into account by the Pillar 1 process (e.g. interest rate risk in the banking book, business and strategic risk); and factors external to the firm (e.g. business cycle effects).

Pillar 3 – aims to encourage market discipline by developing a set of disclosure requirements which will allow market participants to assess key pieces of information on the scope of application, capital, risk exposures, risk assessment process and hence the capital adequacy of the firm.

1.2. Scope of Application

This document represents the Pillar 3 disclosures of Tesco Personal Finance plc ('TPF plc' or the 'Company') which being a Bank and a BIPRU firm it is obliged to provide and is based on disclosure and accounting data for the 12 month period to 28th February 2013.

Tesco Personal Finance Group Limited ('TPFG' or 'TPF Group') is a UK based retail financial services organisation wholly owned by Tesco plc.

Tesco Personal Finance plc, trading as Tesco Bank, is a wholly owned subsidiary of TPFG, which provides a range of financial services and products to personal customers under the Tesco Bank brand, mainly through telephony and on-line sales channels, and through a small number of in-store branches.

The products currently offered by the Company include general insurance products, travel money, unsecured personal loans, secured mortgage advances, savings accounts and credit cards. The Company has limited international exposure, namely in Ireland.

There are no material practical or legal impediments to the prompt transfer of capital resources or repayment of liabilities among the parent and subsidiary members of the TPFG.

Tesco Underwriting Limited ('TU') is 49.9% owned by the Company and 50.1% owned by Ageas (UK) Limited. TU underwrites household and motor insurance and provides claims management for these policies.

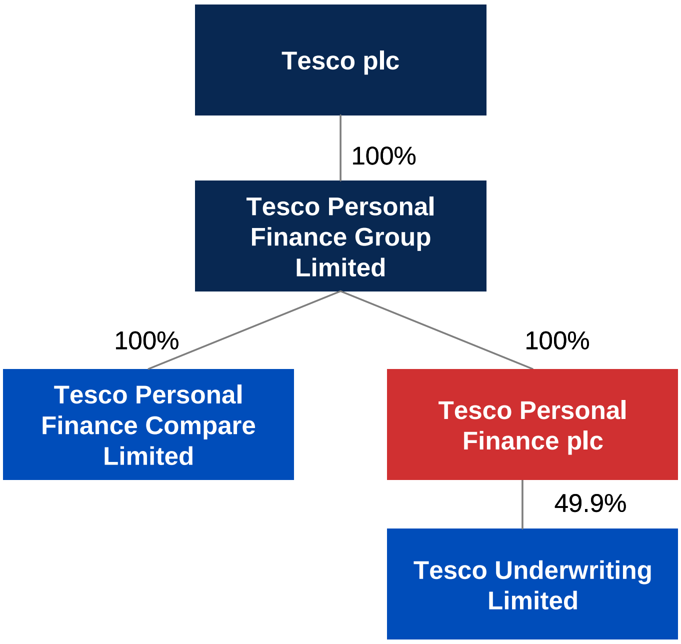
1.2.1. Accounting Consolidation

TPFG operates as a holding company with 100% ownership of the Company and Tesco Compare with the Company holding 49.9% ownership of TU, as illustrated in

Figure 1 below. Financial Statements are produced half- yearly and annually for the Company..

TU is treated as an associate and is proportionally consolidated using the equity method of accounting.

Figure 1: TPF Group Limited: Accounting Consolidation Structure



1.2.2. Prudential Consolidation

The Company does not form part of a Consolidation Group for Regulatory Reporting purposes and does not make use of the solo consolidation waiver provisions.

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1.2.3. Comparison of Pillar 3 Disclosures with the Directors' Report & Financial Statements

These disclosures have been prepared in accordance with Basel II, Pillar 3 regulatory reporting requirements. There are a number of significant differences between accounting disclosure requirements and Pillar 3 disclosure requirements which means that information may not be directly comparable with the Directors' Report and Financial Statements. The main differences for the Company are summarised below:

- Pillar 3 exposure values are reported on the basis of Balance Sheet values, net of provisions where appropriate, with off Balance Sheet exposures assigned credit conversion factors based on prescribed regulatory values which vary according to risk categories;
- Regulatory reporting rules require that the Company make certain deductions from capital resources, the most material of which relate to the subscription for equity and subordinated loans issued by Tesco Underwriting Limited, an insurance associate.

1.3. Disclosure Policy

The following sets out the Company's Disclosure Policy as applied to Basel II Pillar 3 Disclosures, including the information to be disclosed, frequency, media, location and verification.

1.3.1. Information to be disclosed

The Company's policy is to meet all required Pillar 3 disclosure requirements as detailed in Section 11 of the Prudential Sourcebook for Banks, Building Societies and Investment Firms (BIPRU).

1.3.2. Frequency

The Company's policy is to publish the disclosures required on an annual basis. The information is published as soon as practical following publication of the annual Directors' Report and Financial Statements.

1.3.3. Medium and location of publication

The Company's Pillar 3 disclosures are published in the Investors Centre section of the Tesco plc corporate website: www.tescoplc.com/investors/results

1.3.4. Verification

The Company's Pillar 3 disclosures have been reviewed by the Audit Committee and approved by the Board. In addition, the Remuneration disclosures as detailed in Section 14 of this document have been reviewed by the Remuneration Committee. The disclosures are not subject to audit except where they are the same as those prepared under accounting requirements and disclosed in the company's annual Directors' Report and Financial Statements.

2. Document Structure

The document is structured to provide details of Risk Management Objectives and Policy in Section 3. This section is supplemented by a discussion of the Company's "Major Specific Risk Categories" in Sections 6.1, 7, 8, 9, 10, 11 and 12. Capital Resources, the Finance and Treasury Control Framework and Compliance with BIPRU and the overall Pillar 2 rule are considered in Sections 4 and 5. Non Trading Book Exposures in Equities are discussed in Section 10 with Securitisation disclosures published in Section 13. Remuneration disclosures are provided in Section 14.

3. Risk Management Objectives and Policy

3.1. Approach to Risk Management

The Board has overall responsibility for the business. It agrees the strategy for the business, approves the Company's risk appetite as well as specific high level policies and the delegated authorities. Board approval is also required for the Company's business plans, budget, Internal Capital Adequacy Assessment Process (ICAAP), Internal Liquidity Adequacy Assessment (ILAA) and new material product lines. The Board monitor's the Company's risk management profile and capital adequacy position.

Management of profit volatility and development of a stable and prudent business compliant with regulations are amongst the key strategic business objectives. The

Company is focussed on developing a strong savings franchise with reliable sources of funding within an overall culture of treating customers fairly.

The Company seeks to ensure that it has an integrated approach to Risk Management so that all areas of direction setting, organisation and control, decision making, risk appetite, risk identification, risk assessment and business operations are aligned. The Risk Management Framework is described below.

3.2. Risk Management Framework

During the year the Company has worked on the further development of its Risk Management Framework. The principal means by which the Company seeks to deliver effective risk management are contained in the Enterprise Wide Risk Management Framework (EWRMF). The EWRMF is designed to support the identification, assessment, management and control of the material risks that threaten the achievement of the Company's strategic business objectives.

The EWRMF can be broken down into the following five key elements:

1. Risk management strategy and appetite
2. EWRMF components
3. Integrated risk processes
4. Major specific risk categories
5. Embedding risk within the organisation

These are described in further detail in sections 3.3, 3.4, 3.5, 3.6 and 3.7 below.

The EWRMF is documented in the Enterprise Wide Risk Management Manual (EWRMM) which provides a single point of reference in relation to the Company's approach to risk management.

3.3. Risk Management Strategy and Appetite

The Company has clear strategic risk objectives which are defined in relation to Financial Risk, Reputational Risk, Operational and People Risks. Defined Risk Appetite forms a key link between day to day risk management of the business and the company's strategic risk objectives. Risk Appetite defines the type and amount of risk that the company is prepared and not prepared to take to successfully deliver the company's strategic and business objectives.

The Board's high level expression of the desired Risk Appetite is translated into specific risk appetite measures that are tracked, monitored and reported to the appropriate functional Risk Heads, Risk Committees and Board.

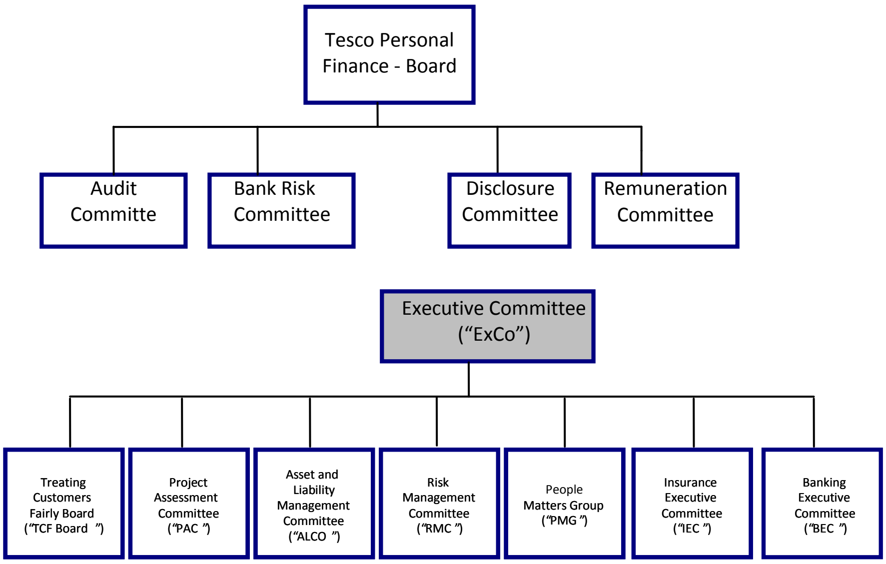
3.4. Enterprise Wide Risk Management Framework Components

The scope of the EWRMF extends to all major specific risk categories faced by the Company and is underpinned by governance, controls, processes, systems and policies within the second-line Risk function and those of the first-line business areas

The key components which collectively ensure that risks are managed and key control activities conducted are outlined below.

3.4.1. Governance

The Board has ultimate responsibility for all material risk matters, but has delegated day to day running of the business to the Chief Executive. The Chief Executive is responsible for delivery of the overall strategy and management of risks and has established the Executive Committee (ExCo) to assist in the management of the business. As an Executive Director and ExCo member the Chief Risk Officer, who is independent from any commercial function, performs a strategic risk management role and is responsible for establishing and enhancing the EWRMF.



A committee structure including BRC, Audit Committee, Remuneration Committee, ExCo, RMC and ALCO operated throughout the year as described below.

- **The Board**

The Board has overall responsibility for the business but has delegated responsibility for day to day running of the business to the Chief Executive who is responsible for setting and developing appropriate strategies to manage risk across the business. The Board comprises an independent non-executive Chair and a further 4 executive directors and 6 non-executive directors.

In order to support effective governance and management of the wide range of responsibilities the Board has established the following three Sub-Committees. These committees are served by members with the most appropriate experience and skill sets

- **(1) Board Risk Committee**

The BRC is comprised of non-executive directors and reports to the Board. The role of the BRC includes the oversight and challenge of the company's risk appetite and the assessment of any future risks and the recommendation to the Board of any changes to Risk Appetite.

- **(2) Audit Committee**

The Audit Committee is comprised of non-executive directors. The role of the Audit Committee includes: reviewing and recommending to the Board for approval the financial statements; monitoring accounting policies and practices for compliance with relevant standards; reviewing the scope and results of the annual external audit; maintaining a professional relationship with and recommending the appointment, re-appointment and removal of the external auditors; examining arrangements in place to enable management to manage risk and to comply with requirements and standards under the regulatory system; overseeing the internal audit function, the internal audit programme and risk assurance programmes and expressing an opinion on the effectiveness of internal controls.

- **(3) Remuneration Committee**

The Remuneration Committee is comprised of non-executive directors. The role of the Remuneration Committee is: to determine and approve remuneration arrangements for Remuneration Code staff. within the Group; to approve a remuneration framework for employees of the Group below the leadership level; to ensure that, where appropriate, remuneration is aligned with Tesco PLC Group Reward Policy; to ensure the levels and structure of remuneration are designed to attract, retain, and motivate the management talent needed to run the Group's business in a way which is consistent with the risk appetite and ongoing sustainability of the business and to be compliant with all applicable legislation, regulation and guidelines.

- **(4) Disclosure Committee**

The Disclosure Committee is comprised of non-executive directors. The role of the Disclosure Committee is to review on behalf of the Board formal company documents which are either destined for publication e.g. Pillar 3, securitisation documents, retail bond documents or which are due to their size and complexity better reviewed in detail in a smaller group than in Board or Board Committee. In addition the Disclosure Committee is responsible for ensuring compliance with relevant legal and regulatory obligations in relation to the timely and accurate disclosure and announcement of information and the treatment of inside information.

- **Executive Committee**

The Tesco Bank Board has delegated day to day running of the business to the Chief Executive, the Chief Executive has established the Executive Committee (ExCo) to assist him manage the business and deliver against the strategy in an effective and controlled way. The ExCo is comprised of the Chief Executive, 3 executive directors and 6 other senior directors. The ExCo provides general executive management of the business and facilitates cross-functional communication and liaison. The relevant ExCo member is responsible to the Chief Executive and through him to the Board, for managing performance in line with the Group's long-term plan, the strategy, the annual budget and the risk appetite.

In order to ensure that high level matters which require cross functional oversight and engagement are dealt with appropriately, the ExCo has established a series of Sub –Committees which report directly to ExCo, the principal ones from a risk perspective being: the Risk Management Committee and the Asset and Liability Committee, their respective roles are detailed hereunder.

- **Risk Management Committee**

The principal role of RMC is to provide oversight, review and challenge of the material risks both current and future affecting the business whilst ensuring that there is effective management and control of all key risks and issues facing the Group. To provide additional support the RMC has established further specialist risk committees for example the Credit Risk Management Committee which is responsible for monitoring the bank's credit performance, maintaining credit risk policy and overseeing credit risk management.

- **Asset and Liability Management Committee**

The principal role of the ALCO is to optimise the Group's balance sheet structure and to identify, manage and control the Group's balance sheet risks, particularly liquidity risk, in the execution of its chosen business strategy. The ALCO has also established specialist committees to support it in the execution of its role for example the Liquidity Manager's Forum which is responsible for monitoring, reviewing and managing the bank's ongoing and forward looking liquidity position.

3.4.2. Three Lines of Defence

The Company's risk management approach follows the 'Three Lines of Defence' model where:

- **First line of defence -** Line Managers are responsible for establishing an effective control framework within their area of operations and identifying and controlling all risks so that they are within the organisational risk appetite and policy limits. They also devise appropriate key risk indicators, management information and assurance processes to render effective the control framework they operate.
- **Second line of defence** - the Risk Management Function is an independent function led by the CRO that provides support and guidance to the first line business areas and is responsible for providing appropriate levels of risk assurance across all business areas
- **Third line of defence** - the Internal Audit function is responsible for the independent assessment of the effectiveness of the implementation of the risk and control measures across the business both in design and practice. They undertake specific reviews of business areas and functions.

3.4.3. Risk Identification

The Risk Identification process sets out to identify and define risk. It provides guidance in relation to the ways in which risks can be identified, the sources to investigate and research in order to identify new and emerging risks and sets out consistent principles which should be applied wherever the Company needs to identify risks.

3.4.4. Risk Assessment

The Risk Assessment process is the means through which the Company understands and estimates the effect of risk on the business and the processes, systems and controls that mitigate those risks to an acceptable level. The Risk Assessment process is the formal method undertaken to determine the potential impact that identified risks or events could have on the Company.

3.4.5. Policies

The Company's policy documents provide the rules and guiding principles that define its approach to control identified risks and are provided as a suite covering all aspects of risk within the EWRMF. The policy framework and accountabilities are the foundations that determine the way the Company has regard to risk when it carries out its business. Detailed accountabilities turn policies and appetite limits into individual limits and responsibilities.

3.4.6. Risk Management Function (RMF)

The RMF operates under the leadership of the CRO who reports directly to the Chief Executive and is a member of ExCo and the Board. The Risk teams reporting to the CRO have been resourced by people with specific expertise and structured to provide analysis, understanding and oversight of each of the major risks faced by the Company.

3.4.7. Stress Testing

Stress Testing is the process under which the Company's business plans are subjected to severe adverse impacts and that the implications of those stresses on the Company's business including projected capital and liquidity positions are understood.

3.4.8. Monitoring and Reporting

The RMF is the focus and centralised location for integrated risk reporting across the Company. The RMF acts as risk integrators to ensure that: risk reporting and communications form a total risk perspective; aggregation and correlation issues are addressed; and risk coverage is viewed holistically so that issues do not fall between other functions.

The Company monitors and tracks current exposures against limits defined in the risk appetite and reports exceptions on a monthly basis to the ALCO and RMC and to each meeting of the BRC. Adherence to these limits is independently monitored, measured and reported using a suite of key indicators defined by each risk team responsible for managing the major specific risk categories faced by the Company. Decisions made at subordinate risk committees and forums are reported up to senior committees as appropriate.

3.5. Integrated Risk Processes

The Company's integrated risk processes include the linking of risk appetite to business plans and associated capital and liquidity requirements.

The Company is required to submit periodic ICAAP reports to the Prudential Regulation Authority (PRA) which set out future plans, their impact on capital availability and requirements and the risks to capital adequacy under potential stress scenarios.

The Company is also required to submit to the PRA an ILAA which provides an ongoing assessment and quantification of the Company's liquidity risks, how the Company mitigates those risks and how much current and future liquidity is required based on business plans and under stress scenarios. The Company must demonstrate that it has sufficient liquidity and contingency plans to manage unexpected cash outflows.

Risk appetite helps to limit the risks which the business can accept in pursuit of its strategic objectives. Risk appetite is formally reviewed annually and is monitored on an ongoing basis for adherence. The Company's strategy, business plan and capital and liquidity plans are set with reference to risk appetite.

The integrated risk process documents define regulatory guidance and requirements, set out expectations and define the processes that are followed in the Company.

3.6. Major Specific Risk Categories

The major specific risk categories are discussed in Sections 6.1, 7, 8, 9, 10, 11 and 12 of this document. Financial and Capital Risk & Controls are discussed in Sections 4 and 5.

3.7. Embedding Risk within the Organisation

Where risk management is effectively embedded, it becomes an intrinsic part of business planning and decision making ensuring that there is no direction taken without considering potential risks and comparing them against the Company's risk appetite.

3.7.1. Risk Culture

A strong company-wide risk culture is an important element of effective risk management. The Company aims to create a culture of risk awareness, openness and incentivisation of correct behaviours. A number of activities are undertaken to ensure consistency of message and appropriate cultural reinforcement. These activities include: non-executive education, briefings by the Risk Management function, modular risk training and reviews of incentive schemes.

3.7.2. Education & Awareness

The Board of Directors is made aware of the major aspects of the Company's risk profile and provides review and challenge to the EWRMF. Building effective awareness is a high-level priority for the Company's risk managers. Risk affects every member of staff and as such they are obliged to manage the risks in their area as part of their line of defence responsibilities. The Company uses a variety of channels to build risk awareness including: Company Intranet; induction and regular risk awareness programmes; Company magazine; risk briefings and general awareness sessions delivered to all levels of management.

3.7.3. Integrated Risk Approach

At a strategic level, the Board and BRC champion the process of risk management and are actively engaged in understanding the risks faced by the Company and in the ongoing monitoring of areas such as the Company's integrated risk processes, its risk profile and the risk management framework. At a tactical level: training ensures appropriate focus on managing risk; business units are required to comply with risk policies; performance is assessed against key risk drivers, limits and variance analysis; and the implementation and review of business operations embodies risk management principles.

3.7.4. Risk Assurance

Risk assurance is undertaken via an integrated risk assurance plan and includes key operational processes with line management adding quality assurance and control checking appropriate to the level of risk the business areas are facing. This is further supported by independent second line oversight where an assurance plan has been worked up. A third line of independent assurance activities is undertaken by the Bank's Internal Audit function.

A quarterly Risk and Control Self Assessment (RCSA) process plays a key role in the Company's approach to risk assurance. RCSA requires each business area to submit their own assurance assessment to the second line Risk team for oversight, review and challenge. As part of the RCSA process, business areas are required to provide evidence to support their assessment and management of key risks and performance of associated controls.

The RMC and the Audit Committee approve the annual Risk Assurance Plan which details business wide assurance review activities undertaken by the Risk Management function.

Additionally the Audit Committee obtain assurance about the internal control and risk management environment through an agreed programme of audits carried out by the Company's Internal Audit function and regular reports from the risk functions. The role and responsibilities of Internal Audit are detailed below.

3.8. Internal Audit

The Internal Audit function supports the Audit Committee in providing an independent assessment of the adequacy and effectiveness of internal controls. Responsibility for Internal Audit within the Company lies with the Audit Director.

The role of Internal Audit is to assess the adequacy and effectiveness of internal systems and controls, procedures and policies. Internal Audit has the following responsibilities:

- to establish, implement and maintain an audit plan to examine and evaluate the adequacy and effectiveness of the Company's systems, internal control mechanisms and arrangements;
- to report control weaknesses identified as a result of work carried out;
- to verify that actions are taken to address the reported control weaknesses; and
- to report to the Audit Committee in relation to internal audit matters.

An Audit Plan is submitted to the Audit Committee for approval on an annual basis. The Audit Director makes regular reports to the Audit Committee on progress against the Audit Plan and key audit findings. The scope of work of Internal Audit covers the whole of the TPF Group, including the Company and Tesco Underwriting. The annual Audit Plan is risk based, focusing on the areas of highest risk.

3.9. Hedging and Mitigating Risk

The Company's Risk Management Framework sets out how risk is managed across the business. Further information in relation to policies, strategies and processes for hedging and mitigating risk are discussed in Sections 5.3, 6.1, 7, 8, 9, 10, 11 and 12 in relation to each of the major specific risk categories.

4. Capital Resources

The Board has ultimate responsibility for the Company's capital management and capital allocation. Day to day responsibility for capital planning and other aspects of capital management are delegated to the Treasurer with stress testing and preparation of the Company's ICAAP falling within the remit of the Chief Risk Officer. The ALCO (chaired by the CEO) is the main body responsible for monitoring all aspects of capital planning and has delegated authority to approve capital injections into subsidiaries of TPFG. The Board is kept informed via a monthly update on the capital plan.

The Finance and Treasury functions are responsible for the Financial Governance of the Company and its Financial, Management, Statutory, Regulatory and Treasury reporting. A number of measures are employed to identify and manage the risks inherent in these processes through the operation of the Company's Risk and Control Self Assessment framework, designed to comply with:

- Statutory, Regulatory and disclosure requirements;
- The Company's policies; and
- First line of defence responsibilities.

The PRA in their capacity as supervisors set targets for, and monitor, the capital adequacy of the Company. Capital adequacy returns are submitted quarterly to the Regulators.

During the 12 month accounting period to 28th February 2013 the Company complied with the capital requirements determined by the PRA.

The table below shows the Company's capital resources as at 28th February 2013.

4.1. Capital Resources

The Company's capital resources are shown in the following table. Information on the composition and main features of the Company's capital resources and components thereof are provided in the following sub-sections.

Capital Resources

Total Capital Resources	February 2013 (£k)	February 2012 Restated (£k)
Core Tier 1 Capital		
Shareholders Equity	1,217,503	1,189,303
Subordinated Notes	(45,000)	(45,000)
Retained Earnings	(18,137)	(83,642)
Unrealised gains on AFS debt securities	(5,762)	(9,505)
Unrealised Gains on Cash Flow Hedge Reserve	(130)	-
	1,148,474	**1,051,156**
Regulatory Deductions		
Intangible Assets	(397,430)	(336,995)
50% of Material Holdings	(63,798)	(53,070)
	(461,228)	**(390,065)**
Core Tier 1	**687,246**	**661,091**
Tier 2 Capital		
Undated Subordinated Notes	45,000	45,000
Dated Subordinated Notes - net of regulatory amortisation	326,500	330,000
Collectively assessed impairment provisions	25,080	21,154
	396,580	**396,154**
Regulatory Deductions		
50% of Material Holdings	(63,798)	(53,070)
	(63,798)	**(53,070)**
Total Tier 2	**332,782**	**343,084**
Other Capital Deductions	-	(258,500)
Total Capital Resources	**1,020,028**	**745,675**
Risk Weighted Assets	**5,353,322**	**4,672,636**
Core Tier 1 Ratio	**12.8%**	**14.1%**
Total Capital Ratio	**19.1%**	**16.0%**

4.1.1. Core Tier 1 Capital

The Company's Tier 1 capital is wholly comprised of Core Tier 1 capital resources. Equity capital comprises share capital and the share premium account. Verified and Other reserves include previously audited Profit and Loss Account reserves, equity capital contribution for Share Based Payment schemes and interim verified profits less dividends paid. The following table shows the movement in Core Tier 1 capital over the year.

Movement in Core Tier 1 Capital

Movement in Core Tier 1 Capital	February 2013 (£k)	February 2012 Restated (£k)
Core Tier 1 at the beginning of the year	661,091	707,681
Ordinary Shares issued	45,000	111,500
Profit attributable to Shareholders	158,025	64,608
Other Reserves	706	7,172
Ordinary Dividends	105,000	108,150
Intangible assets	60,435	121,720
50% of Material Holdings	10,729	-
Core Tier 1 at the end of the year	**687,246**	**661,091**

4.1.2. Hybrid Capital

The Company does not have any forms of hybrid capital.

4.1.3. Deductions from Tier 1 Capital Resources

Intangible assets relate to Computer Software and "Work in Progress" which relates primarily to the internal development of IT software assets in relation to the development of the operational platform.

Material Holdings deduction represents 50% of the investment in TU comprising both equity and subordinated loans

4.1.4. Tier 2 Capital Resources

All dated and undated subordinated debt is issued to TPFG who, in turn, have issued the same amount to Tesco plc. Details of subordinated liabilities are provided in the following table.

Collective provisions are included as Upper Tier 2 capital resources in accordance with GENPRU 2.2.187 to 2.2.189.

Subordinated Liabilities

Subordinated Liabilities	February 2013 (£k)	February 2012 (£k)
Undated floating rate notes issued April 2002	9,000	9,000
Undated floating rate notes issued September 2002	16,000	16,000
Undated floating rate notes issued December 2002	20,000	20,000
Floating rate subordinated loan maturing 2017	30,000	30,000
Floating rate subordinated loan maturing 2018	35,000	35,000
Floating rate subordinated loan maturing 2020	30,000	30,000
Floating rate subordinated loan maturing 2021	140,000	140,000
Floating rate subordinated loan maturing 2022	95,000	95,000
	375,000	375,000

Dated subordinated debt is required to be amortised on a straight line basis over the final five years to maturity.

4.1.5. Capital Resources that provide for an incentive to be redeemed

The undated floating rate notes have no fixed maturity date and may not be repaid except under certain conditions such as the winding up of the Company. The dated floating rate subordinated loans are repayable, in whole or in part, at the option of the issuer, prior to maturity, on conditions governing the debt obligation. Interest payable is based on 3 month LIBOR plus a range of 60 to 225 basis points.

The undated floating rate notes issued in September 2002 and December 2002 had a step up clause which came into effect during the year.

The floating rate note maturing in 2018 contains a step up clause which will come into force in June 2013.

4.1.6. Innovative Tier 1 Capital Resources

The Company does not have any forms of innovative Tier 1 capital resources.

4.1.7. Deductions from Tier 2 Capital Resources

Material Holdings deduction represents 50% of the investment in TU comprising both equity and subordinated loans

4.1.8. Deductions from Total Capital Resources

The loans advanced to RBSI, now the Direct Line Insurance Group (DLG), in support of solvency capital requirements for the insurance products sold under the distribution agreement and underwritten by RBSI were fully repaid during the year.

4.1.9. Tier 3 Capital Resources

The Company does not have any Tier 3 capital resources.

5. Compliance with BIPRU and the overall Pillar 2 Rule

5.1. Approach to assessing adequacy of Internal Capital

Capital is held to provide sufficient resources to absorb losses. The Company aims to maintain a minimum risk asset ratio which will ensure there is sufficient capital to support the risk profile during stressed conditions.

The Company has adopted the Standardised Approaches to the calculation of Pillar 1 minimum capital requirements for Credit and Operational Risk. The Company does not currently have a Trading Book but does calculate a Market Risk position risk requirement in respect of foreign currency in the non-trading book.

Capital adequacy is monitored daily by Treasury with monthly reporting provided to the Board and to the ALCO. In addition, capital planning forms a key element of the Company’s Budgeting and Long Term Plan (LTP) processes. As part of the LTP, the Treasury function prepare a forward looking capital plan covering the current financial year and a further four years which is approved by ALCO and the Board.

The first year of the plan is revised for each reforecast and reported to ALCO and the Board. The capital plan is a living process with the latest iteration submitted monthly to the Board for noting. The capital plan forecasts for the Company show that sufficient capital resources continue to be available to support delivery of business and strategic objectives.

The Bank operates a fully integrated ICAAP process throughout the year that rolls into the final ICAAP assessment. The Bank also performs monthly key risk assessments that include both operational and financial risk stress testing.

External Regulators set ICG for Tesco Bank following completion of the ICAAP which is the Company's internal assessment of capital adequacy designed to address the requirements under Pillar 2 of the Basel II framework.

The ICAAP process considers all of the risks faced by the Company, the likely impact of them if they were to occur, how these risks can be mitigated and the amount of capital that it is prudent to hold against them both currently and in the future. The Company performs a full ICAAP regularly with approval provided by the Board.

Tesco Bank aims to operate at all times over and above the required ICG capital buffer and maintains a prudent level of capital for both short and long term requirements.

5.2. Pillar 1 Capital Requirements

The following table shows the overall Pillar 1 minimum capital requirements and risk weighted assets for the Company under the Standardised Approaches to Credit and Operational Risk. The Company does not operate a Trading Book and therefore has no trading risk exposure. It does calculate a small foreign exchange position risk capital requirement.

Pillar 1 Capital Requirements and Risk Weighted

Minimum Capital Requirements 28 February 2013 (£k)		
Exposure Class	Capital Requirement	Risk Weighted Assets
Central Government and Central Banks	-	-
Multilateral Development Banks	-	-
Institutions	7,761	97,006
Corporates	6,553	81,909
Retail	315,674	3,945,926
Secured by mortgages on residential prop	7,685	96,065
Past due	4,177	52,218
Covered Bonds	336	4,205
Securitisation Positions	385	4,812
Collective Investment undertakings	-	-
Other Assets	13,974	174,668
Total Credit Risk Minimum Capital Requirement under Pillar 1	**356,545**	**4,456,809**
Total Market Risk Minimum Capital Requirement under Pillar 1	**267**	**3,340**
Total Operational Risk Minimum Capital Requirement under Pillar 1	**71,454**	**893,173**
Total Pillar 1 Capital Requirements	**428,266**	**5,353,322**

Minimum Capital Requirements 29 February 2012 (£k)		
Exposure Class	Capital Requirement	Risk Weighted Assets
Central Government and Central Banks	-	-
Multilateral Development Banks	-	-
Institutions	3,673	45,920
Corporates	8,662	108,278
Retail	274,156	3,426,944
Secured by mortgages on residential prop	-	-
Past due	1,858	23,223
Covered Bonds	632	7,905
Securitisation Positions	727	9,085
Collective Investment undertakings	1,491	18,642
Other Assets	18,270	228,372
Total Credit Risk Minimum Capital Requirement under Pillar 1	**309,469**	**3,868,369**
Total Market Risk Minimum Capital Requirement under Pillar 1	**178**	**2,220**
Total Operational Risk Minimum Capital Requirement under Pillar 1	**64,164**	**802,047**
Total Pillar 1 Capital Requirements	**373,811**	**4,672,636**

5.3. Counterparty Credit Risk

Counterparty Credit Risk (CCR) may be defined as the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. Such transactions relate to contracts for financial derivative instruments, securities financing transactions and long settlement transactions. All financial derivative transactions are governed by industry standard International Swaps and Derivatives Association (ISDA) Master Agreements, supplemented by ISDA Credit Support Annexes for a number of counterparties. Information relating to policies used in management of Wholesale Credit Risk, which includes Counterparty Credit Risk, is provided in Section 6.1.2.

As at 28th February 2013 the Company has no public credit rating and therefore has no requirement to post additional collateral in the event of a ratings downgrade. There is also no exposure to credit derivative transactions.

The Company in its ordinary course of business uses over the counter (OTC) derivatives and forward foreign exchange transactions to hedge exposures, i.e. interest rate and foreign exchange risk. The CCR mark to market method is used to measure exposure value and details of exposures are provided in the following table.

Measure for exposure value under the CCR Mark to Market Method

Counterparty Credit Risk Exposures: CCR Mark to Market Method	February 2013 (£k)	February 2012 (£k)
Interest-rate contracts	48,378	33,200
Contracts concerning foreign currency rates and gold	3,049	4,802
Contracts concerning equities	-	-
Contracts concerning precious metals except gold	-	-
Contracts concerning commodities other than precious metals	-	-
Total	**51,427**	**38,002**

Regulatory capital calculations do not incorporate netting benefits and there is no use of collateral in calculating net derivatives credit exposure. This is demonstrated in the following table.

Net Derivative Credit Exposure

Net Derivative Credit Exposure	February 2013 (£k)	February 2012 (£k)
Gross Positive Fair Value of Contracts[1]	33,520	19,522
Less: Netting benefits	-	-
Netted current credit exposure	33,520	19,522
Less: Collateral Held	-	-
Net Derivatives Credit Exposure	**33,520**	**19,522**

[1] Excludes add-on for Potential Future Credit Exposure

6. Credit Risk and Dilution Risk

6.1. Credit Risk

Credit risk is the potential that a bank borrower or counterparty will fail to meet its obligations in accordance with agreed terms. The Company's aim in relation to credit risk is to seek to lend responsibly, ensuring that the credit risk profile remains within agreed volatility parameters.

Credit risk arises principally from the Company's retail lending activities but also from placement of surplus funds with other banks and money market funds, investments in transferable securities and interest rate and foreign exchange derivatives. In addition, credit risk arises from contractual arrangements with third parties where payments and commissions are owed to the Company for short periods of time. Credit risk may also materialise when an adverse change in an entity's credit rating causes a fall in the fair value of the Company's investment in that entity's financial instrument.

The CRO and his direct reports, the Director of Credit Risk and the Insurance & Market Risk Director, are responsible for: the development and oversight of the credit risk management framework; developing credit risk policies, tools and frameworks across the business and instilling a positive risk management culture; managing effective credit risk strategies; providing oversight of credit risk activities undertaken by the first line; and credit performance monitoring.

The Credit Risk function maintains a suite of policies defining the minimum requirements for the management of credit activities across the lifecycle. Credit risk policies include Credit Risk Policy and Minimum Standards, Wholesale Credit Risk Policy, Model Development, Collections and Recoveries, Provisioning and instalment lending. All credit risk policies are subject to annual review by the RMC.

Credit Risk policies are supported by a range of process and procedures manuals that cover the activities undertaken through the credit lifecycle that require manual intervention. Good management information is critical for the effective management of credit risk. A suite of management information is produced for different audiences within the governance framework. Crucial within this suite are Key Risk Indicators, with supporting limits and tolerances, that allow the Company to track performance against appetite and identify any trends that could act as an early warning that performance may move outside risk appetite in the future.

6.1.1. Retail Credit Risk

The Company's credit policy is defined via the credit risk policy and risk appetite framework. Through this, standards and limits are defined at all stages of the customer lifecycle, including new account sanctioning, customer management and collections and recoveries activity. Customer credit decisions are managed principally through the deployment of bespoke credit scorecard models and credit policy rules, which exclude specific areas of lending, and an affordability assessment which determines a customer's ability to repay an outstanding credit amount. Judgemental credit decisions are predominately utilised when assessing mortgage advance applications.

A dedicated credit risk management team have the day to day responsibility for managing the credit quality of the lending portfolio. The Company has full ownership of its credit risk appetite, credit policy and the deployment and execution of credit strategies since credit cards migration completed in May 2012. Responsibility for setting scorecard parameters, and the process for dealing with exceptions, lies with the Director of Credit Risk, reporting to the CRO. Regular reporting to the RMC, ExCo, BRC and the Board provides oversight of this activity and insight to the performance of the portfolio.

6.1.2. Wholesale Credit Risk

The Company does not operate in the mainstream commercial or corporate lending market. However the company is exposed to Wholesale Credit Risk through depositing or lending surplus funds to a number of counterparties, with the inherent risk that these counterparties could fail to meet their obligations. The company therefore maintains a limits-based framework for managing exposure to counterparty credit risk. These limits and the framework are set out in the Wholesale Credit Risk Policy which is approved by the RMC. The Treasury Director is responsible for ensuring that Treasury complies with counterparty credit risk limits, with the Wholesale Credit Risk Manager (within the Market & Liquidity Risk team) and the Insurance & Market Risk Director providing independent oversight that these limits are adhered to.

The control framework defines approved country, counterparty and instrument types and maturity profiles. The Company's risk appetite focuses on counterparties with strong capacity to meet financial commitments and requires approved counterparties to have upper investment grade ratings. Counterparty types include financial institutions, sovereigns and supranationals with approved instrument types including cash, certificates of deposit, bonds, treasury bills, gilts, repurchase agreements, money market funds and asset backed securities / covered bonds. Country limits are derived using External Credit Assessment Institutions (ECAI) ratings and economy size. Interest rate and foreign exchange derivatives are also used to hedge exposures.

The framework sets limits on the amounts that can be lent based on counterparty credit-worthiness, instrument type and remaining tenor. As part of the credit assessment process for wholesale credit risk exposures, the Company continues to use Fitch, Moody's and Standard & Poor's as ECAIs with one of the approved ECAI's used to determine regulatory capital requirements under the Standardised Approach to Credit Risk. The Bank has also set up a Wholesale Credit Risk Forum where current ratings and exposures are discussed on a monthly basis with members of Risk and Treasury attending. Counterparty reviews and proposals for new limits are also discussed at the Forum as well as discussions on current market events and their possible impact on the Bank. All material limits are approved via the RMC and any exceptions or overrides to the Company's policy must be explicitly agreed by the RMC.

Daily monitoring of exposures is undertaken by the Wholesale Credit Risk Manager with monthly reporting of Key Risk Indicators provided to RMC.

As at 28th February 2013 the Company has not recognised any impairment losses in connection with these financial assets. There is therefore no requirement to establish credit reserves for wholesale credit risk exposures.

The Wholesale Credit Risk Policy provides that credit risk mitigation techniques are applied to reduce credit risk exposure. Industry standard ISDA Master Agreements are in place with all derivative counterparties, Global Master Repurchase Agreements are in place for all repurchase agreements and ISDA Credit Support Annexes

(CSA's) have been executed with a number of counterparties with plans in place to have CSA's executed with all derivative counterparties. By Q3 2013 the majority of derivative transactions will be conducted with a clearing house which will reduce our Counterparty exposure on swap transactions. Use is also made of Delivery Versus Payment (DVP) arrangements when settling transactions. As at the end of February 2013 no additional credit risk mitigation has been taken.

6.1.3. Wrong Way Risk

Wrong way risk is defined as the risk that occurs when exposure to a counterparty is adversely correlated with the credit quality of that counterparty.

The Company's Wholesale Credit Risk Policy prohibits the repurchase counterparty and the issuer of the collateral being the same, or related, entities. Where collateral is posted under a derivative CSA the exposure to the issuer of the collateral is managed within the limit framework detailed in Section 6.1.2 above. The Company has no exposure to wrong-way risk.

6.1.4. Third Party Credit Exposures

The Company has a number of contracts with third parties that involve the payment of fees or commissions to TPF plc. Credit exposure arises through the risk that these payments may not be made. The requirements for management of these exposures are detailed in the Wholesale Credit Risk Policy with a limits framework in place to manage these exposures. The Wholesale Credit Risk Manager is responsible for reporting these exposures and any limit breaches to RMC.

6.1.5. Credit Risk: Analysis by Exposure Class

The table below shows the credit risk exposure at the financial year end together with average credit risk exposure for the financial year.

This may differ from the amounts disclosed in the balance sheet in the Annual Report and Accounts, as it includes amounts where the customer has a contractual right to draw down further balances, converted using regulatory credit conversion factors.

The exposure is shown gross before taking into account the effects of credit risk mitigation but is reported net of appropriate impairment provisions.

Credit Risk: Analysis by Exposure Class

Exposure Class	Exposure Value		Average Exposure Value	
	February 2013 (£k)	February 2012 (£k)	Mar 12 - Feb 13 (£k)	Mar 11 - Feb 12 (£k)
Central Governments or Central Banks	1,349,612	1,239,934	1,386,723	1,021,137
Multilateral Development Banks	301,388	386,078	323,427	326,054
Institutions	229,642	130,606	174,925	232,176
Corporates	154,564	108,848	95,508	151,088
Retail Claims	5,261,235	4,569,259	4,896,822	4,715,636
Secured by mortgages on residential property	274,471	-	22,873	-
Past Due Items	52,218	23,223	39,013	9,696
Covered Bonds	21,026	39,526	27,431	6,075
Securitisation Positions	24,058	45,423	26,391	51,648
Collective Investment Undertaking	-	93,209	149,706	135,707
Other	283,954	260,076	229,284	244,819
Total	**7,952,168**	**6,896,182**	**7,372,103**	**6,894,036**

6.1.6. External Credit Assessment Institutions' Assessments

The table below shows the credit risk exposure by Credit Quality Step.

Issue credit assessments are used for investments in specific obligations, mainly Asset Backed Securities / Covered Bonds and Government Guaranteed Bonds, where there are adjustments to the issuer's general rating that reflect factors specific to the investment.

Issuer credit assessments are generally used for other forms of lending where the assessment concerns the general capacity and willingness of the counterparty to meet their obligations. Ratings are obtained from market sources with processes in place to assign appropriate ratings to exposures and to monitor rating actions. The Company complies with the credit quality assessment scale with the appropriate issue or issuer rating used to determine the risk weights applied under the Standardised Approach to Credit Risk. Capital is assigned according to BIPRU requirements as explained in Section 5 above.

Analysis of Exposures by Credit Quality Step

Exposure Values 2013	Credit Quality Step 1 (£k)	Credit Quality Step 2 (£k)	Credit Quality Step 3 (£k)	Credit Quality Step 4 (£k)	Credit Quality Step 5 (£k)	Credit Quality Step 6 (£k)	Unrated (£k)	Total (£k)
Fitch Assessment	**AAA to AA-**	**A+ to A-**	**BBB+ to BBB-**	**BB+ to BB-**	**B+ to B-**	**CCC+ and below**		
Central Governments or Central Banks	1,349,612							1,349,612
Multilateral Development Banks	301,388							301,388
Institutions	27,247	202,383	12					229,642
Corporates	2	145,307	2,789				6,466	154,564
Retail Claims							5,261,235	5,261,235
Secured by mortgages on residential property							274,471	274,471
Past Due Items							52,218	52,218
Covered Bonds		21,026						21,026
Securitisation Positions	24,058							24,058
Collective Investment Undertaking	-							-
Other							283,954	283,954
Total exposures pre mitigation	**1,702,307**	**368,716**	**2,801**	**-**	**-**	**-**	**5,878,344**	**7,952,168**
Total exposures post mitigation	**1,702,307**	**368,716**	**2,801**	**-**	**-**	**-**	**5,878,344**	**7,952,168**

Exposure Values 2012	Credit Quality Step 1 (£k)	Credit Quality Step 2 (£k)	Credit Quality Step 3 (£k)	Credit Quality Step 4 (£k)	Credit Quality Step 5 (£k)	Credit Quality Step 6 (£k)	Unrated (£k)	Total (£k)
Fitch Assessment	**AAA to AA-**	**A+ to A-**	**BBB+ to BBB-**	**BB+ to BB-**	**B+ to B-**	**CCC+ and below**		
Central Governments or Central Banks	1,239,934							1,239,934
Multilateral Development Banks	386,078							386,078
Institutions	17,644	112,962						130,606
Corporates		1,140	15,922				91,786	108,848
Retail Claims							4,569,259	4,569,259
Secured by mortgages on residential property							-	-
Past Due Items							23,223	23,223
Covered Bonds		39,526						39,526
Securitisation Positions	45,423							45,423
Collective Investment Undertaking	93,209							93,209
Other							260,076	260,076
Total exposures pre mitigation	**1,782,288**	**153,628**	**15,922**	**-**	**-**	**-**	**4,944,344**	**6,896,182**
Total exposures post mitigation	**1,782,288**	**153,628**	**15,922**	**-**	**-**	**-**	**4,944,344**	**6,896,182**

6.1.7. Credit Risk: Analysis by Geography

The table below provides the geographic distribution of the Company's credit risk exposure.

The Company is primarily focussed on providing financial services and products to UK personal customers although there is limited exposure in the Republic of Ireland. The Company sells credit cards into the Republic of Ireland where it is an authorised 'credit institution' under Irish law and is directly regulated by the Irish Financial Regulator in respect of this activity.

Credit Risk: Analysis by Geography

Exposure Class	Geographic Location (28 February 2013)			
	UK (£k)	Europe (ex. UK) (£k)	Other (£k)	Total (£k)
Central Governments or Central Banks	1,198,648	150,964	-	1,349,612
Multilateral Development Banks		196,223	105,165	301,388
Institutions	229,642			229,642
Corporates	154,475	89	-	154,564
Retail Claims	5,226,280	34,955		5,261,235
Secured by mortgages on residential property	274,471			274,471
Past Due Items	51,288	930		52,218
Covered Bonds	21,026			21,026
Securitisation Positions	24,058			24,058
Collective Investment Undertaking	-	-		-
Other	283,954			283,954
Total	**7,463,842**	**383,161**	**105,165**	**7,952,168**

Exposure Class	Geographic Location (28 February 2012)			
	UK (£k)	Europe (ex. UK) (£k)	Other (£k)	Total (£k)
Central Governments or Central Banks	1,011,565	220,963	7,406	1,239,934
Multilateral Development Banks		288,457	97,621	386,078
Institutions	130,606			130,606
Corporates	108,116	348	384	108,848
Retail Claims	4,537,419	31,840		4,569,259
Secured by mortgages on residential property				-
Past Due Items	23,168	55		23,223
Covered Bonds	39,526			39,526
Securitisation Positions	45,423			45,423
Collective Investment Undertaking	50,035	43,174		93,209
Other	260,076			260,076
Total	**6,205,934**	**584,837**	**105,411**	**6,896,182**

6.1.8. Credit Risk: Analysis by Industry type

The distribution of credit risk exposure by industry type is provided in the following table.

The Company is primarily focussed on providing financial services and products to UK personal customers although it also has exposure to wholesale counterparties as detailed in Section 6.1.2 above.

Credit Risk: Analysis by Industry Type

Exposure Class	Financial Institutions (£k)	Government (£k)	Individuals (£k)	Wholesale and retail trade (£k)	Total (£k)
	Industry Type (28 February 2013)				
Central Governments or Central Banks		1,349,612			1,349,612
Multilateral Development Banks	301,388				301,388
Institutions	229,642				229,642
Corporates				154,564	154,564
Retail Claims			5,261,235		5,261,235
Secured by mortgages on residential property			274,471		274,471
Past Due Items			52,218		52,218
Covered Bonds	21,026				21,026
Securitisation Positions	24,058				24,058
Collective Investment Undertaking	-				-
Total	**576,114**	**1,349,612**	**5,587,924**	**154,564**	**7,668,214**

Exposure Class	Financial Institutions (£k)	Government (£k)	Individuals (£k)	Wholesale and retail trade (£k)	Total (£k)
	Industry Type (29 February 2012)				
Central Governments or Central Banks		1,239,934			1,239,934
Multilateral Development Banks	386,078				386,078
Institutions	130,606				130,606
Corporates				108,848	108,848
Retail Claims			4,569,259		4,569,259
Secured by mortgages on residential property			-		-
Past Due Items			23,223		23,223
Covered Bonds	39,526				39,526
Securitisation Positions	45,423				45,423
Collective Investment Undertaking	93,209				93,209
Total	**694,842**	**1,239,934**	**4,592,482**	**108,848**	**6,636,106**

Note that Other Assets have been excluded from these tables.

6.1.9. Credit Risk: Exposure by Residual Maturity

An analysis of residual maturity of exposures, on a contractual basis, is provided in the following table.

Credit Risk exposure by residual maturity

Exposure Class	On Demand (£k)	Repayable in 3 months or less (£k)	Repayable between 3 months and 1 year (£k)	Repayable between 1 and 5 years (£k)	Repayable over 5 years (£k)	Undated (£k)	Total (£k)
	Residual Maturity (Contractual) (28 February 2013)						
Central Governments or Central Banks	867,271	3,733	8,500	349,882	114,850	5,376	1,349,612
Multilateral Development Banks		449	52,060	206,197	42,682		301,388
Institutions		58,373	120,433	10,222	40,614		229,642
Corporates		154,564					154,564
Retail Claims	2,776,043	250,317	586,682	1,479,051	169,142		5,261,235
Secured by mortgages on residential property		1,998	8,135	33,996	230,342		274,471
Past Due Items	29,110	3,407	8,391	11,310	-		52,218
Covered Bonds		45		20,981			21,026
Securitisation Positions		172		23,886			24,058
Collective Investment Undertaking							-
Other						283,954	283,954
Total	**3,672,424**	**473,058**	**784,201**	**2,135,525**	**597,630**	**289,330**	**7,952,168**

Exposure Class	On Demand (£k)	Repayable in 3 months or less (£k)	Repayable between 3 months and 1 year (£k)	Repayable between 1 and 5 years (£k)	Repayable over 5 years (£k)	Undated (£k)	Total (£k)
	Residual Maturity (Contractual) (29 February 2012)						
Central Governments or Central Banks	424,101	40,136	76,980	398,503	295,126	5,088	1,239,934
Multilateral Development Banks		22,117	24,715	234,766	104,480		386,078
Institutions		58,928	36,606	9,311	25,761		130,606
Corporates		108,848					108,848
Retail Claims	2,429,845	259,229	507,392	1,236,859	135,934		4,569,259
Secured by mortgages on residential property							-
Past Due Items	2,236	6,918	4,985	8,495	589		23,223
Covered Bonds		137		26,924	12,465		39,526
Securitisation Positions		7,947		27,789	9,687		45,423
Collective Investment Undertaking	93,132	77					93,209
Other						260,076	260,076
Total	**2,949,314**	**504,337**	**650,678**	**1,942,647**	**584,042**	**265,164**	**6,896,182**

6.1.10. Credit Risk: Past Due and Impaired Assets

The Company considers exposures to be past due where a customer does not make their minimum contractual monthly payment. For accounting purposes, an asset is considered to be impaired where there is objective evidence of impairment (for example, bankruptcy, insolvency, reposession or a declaration of financial hardship) or for unsecured products where a customer is more than 90 days past due in interest or principle items. For the secured portfolio the days past due count is taken to be 180 days.

Details of past due and impaired exposures (gross of provisions), value adjustments and provisions and the net charge for the period, by industry type together with details of past due and impaired exposures by geography are provided in the following tables.

Past Due and Impaired Exposures by Industry

	Financial Institutions (£k)	Governments (£k)	Individuals - Unsecured (£k)	Individuals - Secured (£k)	Individuals - Insurance Installment (£k)	Wholesale and retail trade (£k)	Total (£k)
	Impaired and Past Due exposures by Industry Type 28 February 2013						
Past Due not Impaired							
0-29 days	-	-	40,483	243	1,125	-	41,851
30-59 days	-	-	10,465	-	256	-	10,721
60-119 days	-	-	8,970	-	17	-	8,987
Total	-	-	59,918	243	1,398	-	61,559
Impaired Exposures	-	-	184,934	-	-	-	184,934
Impairment Provisions	-	-	172,100	50	-	-	172,150
Net Impairment Charge	-	-	73,100	50	-	-	73,150

Impaired and Past Due exposures by Industry Type 29 February 2012 (restated)	Financial Institutions (£k)	Governments (£k)	Individuals - Unsecured (£k)	Individuals - Secured (£k)	Individuals - Insurance Installment (£k)	Wholesale and retail trade (£k)	Total (£k)
Past Due not Impaired							
0-29 days	-	-	45,823	-	1,192	-	47,015
30-59 days	-	-	13,789	-	230	-	14,019
60-119 days	-	-	13,527	-	80	-	13,607
Total	-	-	73,139	-	1,502	-	74,641
Impaired Exposures	-	-	194,422	-	-	-	194,422
Impairment Provisions	-	-	184,631	-	-	-	184,631
Net Impairment Charge	-	-	119,028	-	-	-	119,028

Past Due and Impaired Exposures by Geography

Impaired and Past Due exposures by Georgraphy 28 February 2013	UK (£k)	Europe (ex. UK) (£k)	Other (£k)	Total (£k)
Past Due not Impaired				
0-29 days	40,873	978	-	41,851
30-59 days	9,593	1,128	-	10,721
60-119 days	7,258	1,729	-	8,987
Total	57,724	3,835	-	61,559
Impaired Exposures	180,548	4,386	-	184,934
Impairment Provisions	168,720	3,430	-	172,150
Net Impairment Charge	71,115	2,035	-	73,150

Impaired and Past Due exposures by Georgraphy 29 February 2012 (restated)	UK (£k)	Europe (ex. UK) (£k)	Other (£k)	Total (£k)
Past Due not Impaired				
0-29 days	44,633	2,382	-	47,015
30-59 days	13,432	587	-	14,019
60-119 days	13,416	191	-	13,607
Total	71,481	3,160	-	74,641
Impaired Exposures	190,921	3,501	-	194,422
Impairment Provisions	181,326	3,305	-	184,631
Net Impairment Charge	117,650	1,378	-	119,028

6.1.11. Credit Risk: Value Adjustments and Provisions

Credit risk provisioning and impairment is the responsibility of the Board. Day to day responsibility for impairment provisions lies with the Chief Financial Officer and the Chief Risk Officer.

In managing credit risk provisioning and impairment the Company apply IFRS, specifically International Accounting Standard 39: Financial Instruments (IAS 39) which requires that financial assets are assessed for impairment. Loan impairment provisions are established to recognise incurred impairment losses. A loan is impaired when 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.

The Company applies a collective impairment provisioning model that segments provisions into the incurred but not reported (non-defaulted) book and the defaulted (bad) book based upon the approved definition of default operated on the credit card, loan and mortgage portfolios. Incurred but not reported provisions are held where there is objective evidence of impairment on an account (e.g. missed payments) but the account does not yet meet the Company's definition of default. Impairment provisions are established on a portfolio basis taking into account the level of arrears, security, past loss experience and defaults based on portfolio trends. The most significant factors in establishing these provisions are the expected loss rates.

The undernoted table shows the reconciliation of changes in provisions for loans and advances. This table excludes impairment losses of £8,863k (2012 £5,483k) arising on amounts due from the insurance business.

Analysis of Impairment provisions for loans and advances

	28/02/2013 £'000	29/02/2012 £'000
At beginning of the year	184,631	181,821
Amounts written off	(93,627)	(120,187)
Recoveries of amounts previously written off	10,787	7,811
Charge to income statement	73,150	119,028
Unwind of discount	(2,791)	(3,842)
At end of year	172,150	184,631

Provisions for impaired loans and advances at 28th February 2013 were £147,071k (2012: £163,477k).

There are no further value adjustments in relation to credit risk. Non-credit risk value adjustments are disclosed in Note 19 of the Directors' Report and Financial Statements.

6.1.12. Credit Risk Mitigation

Policies are in place which allow the use of credit risk mitigation to reduce Counterparty Credit Risk. As at end February 2013 no use has been made of collateral other than industry standard ISDA agreements, ISDA Credit Support Annexes used in relation to financial derivative transactions and Global Master Repurchase Agreements used in relation to repurchase transactions. Similarly, the Company has not made use of on or off-balance sheet netting.

6.2. Dilution Risk

The Company has no exposure to dilution risk.

7. Market Risk

Market risk is defined as the risk that the value of the Company's income, liabilities, assets or costs might vary due to changes in the value of financial market prices; this includes interest rates, foreign exchange rates, credit spreads and equities. The Company has no Trading Book. Market risk arises in the following ways in the Company:

- Interest rate risk in the Company's retail portfolios, its ATM income and in its funding activities arises from the different repricing characteristics of non-trading assets and liabilities, hereafter referred to as interest rate risk in the banking book (IRRBB);
- Foreign exchange exposures that arise from foreign currency investments, foreign currency loans, deposits, income and other foreign currency contracts;
- Interest rate and credit spread risk in the investment portfolios of the Company's insurance company Tesco Underwriting (TU); and
- Investment risk relating to the Company's pension obligations.

Control of market risk exposure is managed by ALCO, and there are also regular reports to the RMC and Board. The Bank has also established the Market Risk Forum (MRF) where monitoring, review and proposal of pro-active action relating to the Bank's market risk positions on a detailed level occurs. The MRF discusses papers and proposals for approval the week prior to each ALCO, with membership comprised of senior members of the Treasury and Market & Liquidity Risk (M&LR) teams. In addition, the M&LR team provides review and challenge of policies and procedures relating to market risk across the Company on an ongoing basis. M&LR are responsible for oversight of the Asset & Liability Management (ALM) and Market Execution teams within Treasury.

7.1. Interest Rate Risk in the Banking Book

IRRBB is the main market risk that could affect the Company's net interest income and arises where there is potential for changes in benchmark interest rates (that embed little or no credit risk) which results in a movement in the Banking Book net interest income.

- IRRBB may arise for a number of reasons, for example:
- Repricing Risk – related to the timing differences in the maturity (for fixed rate) and repricing (for floating rate) of the Company's assets, liabilities and off balance sheet positions;

- Yield Curve Risk - risk that earnings from banking book products are adversely affected by movement in the yield curve due to the timing mismatch in the repricing of assets, liabilities and off balance sheet positions;
- Basis Risk - risk arising from the imperfect correlation between changes in interest rate indices, such as between LIBOR and Base rate or between Base rate and Administered rates;
- Customer Optionality – risk that a loss in value arises because the take up of a fixed rate product, e.g. personal fixed rate loans, are different from expectations (recruitment risk) or the repayment behaviour of customers, e.g. mortgages, differs from expectations (prepayment risk), due to, or combined with, a movement in interest rates.

The Company has established limits that describe its risk appetite in this area and stress tests are performed using sensitivity to fluctuations in underlying interest rates in order to monitor this risk. The Board have delegated authority for detailed approval of IRRBB to the ALCO. High level risk appetite and policies are recommended for approval by the ALCO to the Board. The ALCO have delegated responsibility to the ALM team to ensure that the Company's IRRBB Risk Appetite is effectively managed. The Market Risk Forum and the M&LR team provide the governance and oversight relating to ALM's management of the IRRBB. The IRRBB policy is owned and monitored by Treasury and approved by ALCO. The main policy objectives are to:

1. Manage the overall IRRBB of the Company by:
    - Identifying, assessing, controlling and reporting the Company's interest rate risk exposure within risk appetite parameters;
    - Minimising the sensitivity at product, balance or business level of net interest income to changes in benchmark interest rates; and
    - Ensuring that IRRBB arising in the Company is transferred to the market or managed efficiently by Treasury within approved limits.
2. Ensure that compliance with evolving regulatory IRRBB requirements is maintained within each jurisdiction in which the Company operates, including requirements set out as part of the ICAAP process.

Non traded interest rate risk primarily arises from the consumer lending portfolios (including the mortgage pipeline) and retail deposits. Hedging strategies are implemented as required to ensure that the Company remains within stated risk appetite.

The main hedging instruments used are interest rate swaps and the residual exposure is reported to the ALCO monthly using two key risk measures:

- Economic value of equity sensitivity to 200 basis point movements across the yield curve. This is then expressed as a percentage change from the base present value of equity; and
- Net interest income sensitivity to an instantaneous 1% parallel movement in interest rates.

The different methodologies can be summarised as:

Economic Value of Equity (EVE) – the EVE approach focuses on the value of the Company in today's interest rate environment and its sensitivity to changes in interest rates. This is done by scheduling the cash flows of all assets and liabilities and applying a set of discount rates to develop the present values. The present value of equity is derived by calculating the difference between the present value of assets and liabilities (Equity = Assets - Liabilities). The EVE calculation for the Company is subject to sensitivity analysis comprising +200 and -200 basis point movements across the yield curve. This is then expressed as a percentage change from the base present value of equity.

Net Interest Income (NII) Sensitivity – This measures the effect of a 100 basis point parallel interest rate shock on the next 12 months NII, based on the re-pricing gaps in the existing portfolio.

Measure	February 2013	February 2012
Economic Value of Equity (EVE)	(6.51%)	(7.84%)
NII Sensitivity	(0.58%)	(1.26%)

7.2. Foreign Exchange Risk

The Company invests in non-GBP denominated bonds, and may raise funding from the wholesale markets in currencies other than GBP. Foreign exchange (FX) exposure arises if these exposures are not hedged. FX exposure may also arise through the Company's EUR-denominated Irish credit card exposure, through the cash held in tills and in transit from the Travel Money business and through invoices received which are denominated in foreign currencies.

All foreign currency exposure is hedged such that no material net exposure results. This exposure is reflected in the foreign currency position risk requirement detailed in Section 5.2 above.

7.3. Tesco Underwriting Investment Portfolios

Tesco Bank is indirectly exposed to Market Risk through its ownership of 49.9% of Tesco Underwriting Limited (TU).

The TU investment portfolio is predominantly comprised of bonds, with the residual amount consisting of short term cash investments.

The main risks in the portfolio relates to changes in: (i) interest rates affecting fair value arising as a proportion of the bonds are fixed rate in nature, (ii) credit quality, as the range of assets held are issued by a variety of institutions with different credit characteristics.

Portfolio management is undertaken by the TU investment committees. The Company's ALM team monitors high-level risk information and the performance of the portfolios and reports this to the ALCO on a monthly basis. Market & Liquidity Risk provides oversight and challenge.

7.4. Pension Risk

Pension Risk may be defined as: the risk to a company caused by its contractual or other liabilities to or with respect to a pension scheme (whether established for its employees or those of a related company or otherwise).

The Company is a participating employer in the Tesco plc Pension Scheme (the Scheme) which is accounted for on a contributions only basis as described in Note 39 to the Company's Directors' Report and Financial Statements.

8. Liquidity and Funding Risk

Liquidity risk is the risk that the Group has insufficient cash resources to meet its obligations as they fall due or can do so only at excessive cost. Liquidity adequacy is the on-going ability to accommodate liability maturities and withdrawals, fund asset growth, and otherwise meet contractual obligations through unconstrained access to adequate funding resources at reasonable market rates. The Group seeks to maintain a conservative liquidity and funding profile ensuring that it is able to meet its financial obligations under normal and stressed market conditions.

The Board determines and approves the Liquidity Risk Appetite of the bank. It also reviews and approves the bank Liquidity Risk Management Policy framework (LRMP) and delegates to the CEO and thence, through ExCo and the ALCO, the day to day responsibility for complying with the framework which is in turn delegated to the Treasurer. The LRMP provides a framework to enable the Group to manage liquidity risk in a structured and prudent manner, as approved by the Board.

The Treasurer is responsible for ensuring that all liquidity and funding measures are managed within policy and appetite. Liquidity management information is provided on a regular basis to the Liquidity Management Forum, the ALCO and the Board, with any exceptions highlighted. The Market and Liquidity Risk team provides review and challenge of policies and procedures relating to funding and liquidity risk.

The Treasurer is also responsible for formulating, and obtaining Board approval for, an annual funding plan as part of the overall business planning process. This ensures that the longer term growth plans of the business can be accommodated within and from available sources of funding whilst maintaining the liquidity risk profile of the bank within the Board approved risk appetite.

The Bank sets formal limits within the LRMP to maintain liquidity risk exposures within the Liquidity Risk Appetite set by the Board. The key liquidity measures monitored on a daily basis are the Internal Liquidity Requirement (ILR), Individual Liquidity Guidance (ILG) ratio, the Net Stable Funding Ratio (NSFR) and the Net Wholesale Funding Outflow. The ILR requires the Group to maintain sufficient liquid assets to survive a defined stress scenario (which the Company defines as a "severe retail run") for a 90 day period. The statutory ILG ratio requires the Group to maintain sufficient high quality liquid assets to meet liquidity requirements during periods of market dislocation and stress. The NSFR measure is designed to enable the Group to fully fund long term and illiquid assets by an appropriate combination (size and maturity) of stable liabilities. The ratio does not give any credit for short-term wholesale funding thereby lessening refinancing risk. Management of the Net Wholesale Funding Outflow is designed to restrict high concentrations of wholesale cash outflows and to spread wholesale funding maturities.

Additionally, the bank monitors and reports on the composition of its funding base against defined thresholds to avoid funding source and maturity concentration risks.

Levels of asset encumbrance are also controlled within pre-determined limits and are reported to ALCO. During 2013 the bank did not make use of collateralised funding facilities. Going forward the bank will be utilising pools of assets to access collateralised funding facilities which have been established by the Bank of England – FLS and DWF.

Stress testing and reverse stress testing of current and forecast Balance Sheets is conducted to inform the Group of required liquidity resources and the circumstances that would result in liquidity resources being exhausted.

9. Operational Risk

Operational Risk is the potential error, loss, harm or failure caused by ineffective or inadequately defined processes, system failure, improper conduct, human error or from external events. The Company aims to minimise all operational risks and reputational impacts.

The CRO, and his direct report, the Head of Operational Risk, are responsible for: developing and maintaining the operational risk framework; working with the business to ensure they understand their first line responsibilities and how they must execute them within the framework; embedding policies, tools and frameworks across the business and instilling a positive risk management culture; and independently monitoring, assessing and reporting on operational risk profiles and losses. In addition, the Head of Operational Risk also has responsibility for second line of defence fraud risk management (internal and external to the business), anti-money laundering (AML) and information security.

One of the biggest operational risks run by the Company over the past three years has been the Transformation programme under which the Company has set up infrastructure and processes separate from RBS. This activity has now been completed with the migration of the Company's credit card business from RBS in May 2012. In addition, the mortgage lending platform went live from August 2012. The Company is now working towards the introduction of a current account during 2014.

The Company assesses its operational risk capital requirement using the Standardised Approach.

10. Non trading book exposures in Equities

The Company's non trading exposure in equities relates to the investment in TU who underwrite Motor and Home insurance contracts under the Tesco Bank brand. TU is an associate of the Company which has a 49.9% equity share. This equity position in the non-trading book is held for strategic objectives. The Company values the investment in TU at cost less any provision for impairment. At 28th February 2013 this investment was valued at £86,013k (2012 £71,708k) and accounted for all non-trading book equities.

11. Insurance Risk

The Company defines insurance risk as the risk accepted through insurance products in return for a premium. These risks may or may not occur and the amount and timing of these risks are uncertain and determined by events outside of our control (e.g. flood or car crash). The Company's aim is to actively manage insurance risk exposure with particular focus on those risks that impact profit volatility.

Insurance risk is typically categorised in the following way:

Underwriting risk – Related to the selection and pricing (or quantification) of the risk currently being transferred from customers to an insurer; and

Reserving risk – Related to valuation and management of financial resources sufficient to pay claims for the risk already transferred from customers to an insurer.

The Company has no direct insurance risk however it is indirectly exposed to insurance risk through its ownership of 49.9% of TU, an authorised insurance company. Historically, the Company had a distribution arrangement with DLG under which the Company carried insurance risk but this arrangement has now terminated and all insurance risk under that arrangement has transferred to RBS under the terms of a termination agreement.

Since late 2010 the majority of new and renewal business policies for Home and Motor Insurance products sold by the Company have been underwritten by TU. The Company provides marketing, sales and distribution of these products with TU providing underwriting, reserving and claims management. The key insurance risks within TU relate to Underwriting Risk and Reserving Risk and specifically the potential for a major weather event to generate significant claims on Home insurance or the cost of settling bodily injury claims on Motor insurance. Exposure to these risks, and pricing risks, are actively managed within TU with close monitoring of performance metrics and the use of reinsurance to limit TU's exposure above pre-determined limits. The Company conducts oversight of these exposures as a significant shareholder in TU.

Additional capacity is provided by a panel of third party providers for Motor and Home customers. The Company also markets Pet, Travel, Life, Health, Dental, Commercial Van and Breakdown insurance on a "white label" basis for other providers. In addition, during the course of this year the Company launched a new payment protection product, sold on a "white label" basis by another provider. The Company does not carry the insurance risk associated with these products, which remains with the provider.

The Company is no longer exposed to Reserving Risk through its previous relationship with DLG– i.e. the risk that claims reserves are insufficient to cover the ultimate cost of those insurance claims that have not yet been settled. Under the terms of the termination agreement with RBS and DLG all insurance risk, under that arrangement, transfers to them.

In addition, the Company migrated the PPI back book for credit cards to the new provider Cardif Pinnicle. However, the single premium loan book remained with DLG..

The insurance risk team is responsible for designing and implementing the insurance risk framework which seeks to: provide an effective and consistent approach to insurance risk management and to the management of insurance counterparties, including TU and white label providers; understand and manage the potential volatility of the insurance results; measure the extent to which the insurance business within the Company is being conducted in accordance with the risk appetite and policies; to provide subject matter expert support to the business in identifying, assessing and managing risk in accordance with the Company's EWRMF; and to monitor the performance of TU and the effectiveness of insurance risk management.

TU is responsible for its Individual Capital Assessment (ICA) as a subsidiary of Ageas. TU operates a separate risk framework with dedicated risk and compliance teams and a suite of TU risk policies. TU is working to implement Solvency II in accordance with regulatory timelines. Solvency II aims to establish an enhanced set of capital and risk management standards across the European insurance industry.

12. Legal and Regulatory Compliance Risk

Legal & regulatory compliance risk is the risk of consequences arising as a result of non-compliance with the laws and regulations affecting the Company's governance, prudential arrangements, business activities, risk management and its conduct with customers. The Company's aim is to meet all legal and regulatory requirements and minimise any reputational impact by maintaining an effective control framework. Where legal or regulatory requirements are not met effective remediation plans will be put in place.

The CRO, and his direct report, the Director of Compliance & Regulatory Risk, together with a dedicated Regulatory Risk team are responsible for: regulatory risk management policies and processes; ensuring that regulatory risks are identified and managed appropriately; monitoring, challenge and oversight of regulatory risk and compliance across the Company's business; and providing guidance and advice to enable the business to operate in a compliant manner. Regulatory Risk's scope includes FCA and PRA regulations as well as the Office of the Information Commissioners requirements (for the Data Protection Act) as well as internal regulatory risk management policies.

As part of the Company's Policy Framework approach, Regulatory Risk is responsible for the Compliance Policy which is approved by the Company's board. The Compliance Policy sets out the scope of the Company's regulatory responsibilities and its approach to managing regulatory risk across the business. Regulatory Risk are also responsible for the detailed regulatory policies that are already in place and that will underpin the Compliance policy (e.g. Data Protection and Regulatory Contact) which are approved through RMC. These will be further supported by Operational Guides that provide relevant practical guidance to business and operational areas to enable them to comply with the regulatory policies which are currently in development.

The Company's Legal function provides advice and support on all aspects of law and associated policies, including Statutory Compliance Policy, Competition Policy, Bribery and Corruption and Information Retention.

13. Securitisation and Covered Bonds

13.1. Securitisation and Covered Bond Roles, Objectives, Involvement and Accounting Treatment

The Company has acted as an originator of securitisations, for the purpose of accessing the Bank of England's Special Liquidity Scheme. As at 28th February 2013 the Company's securitisation programme 'Delamare Cards MTN Issuer Plc' holds £1,884m (2012: £1,224m) of originated credit card receivables on trust for the sole benefit of the Company

The Company also operates within the securitisation and covered bond markets as an investor, purchasing certain securitisation and covered bond issuances for the purposes of diversifying its wholesale assets as part of managing its overall diversified funding plan. As an investor, the Company invests directly in third party asset backed securities and it does not hold any re-securitisation positions.

The Company does not act as a sponsor to any securitisations and it does not provide liquidity facilities to either originated asset backed securities or any third parties involved in securitisation activity.

The Company's involvement in securitisation and covered bond activity is summarised in the following table.

Securitisation and Covered Bond Involvement

Total Outstanding Securitisation Exposure as at 29 February 2013				
Securitisation Role / Exposure Type	Exposure Value (£k)	Impaired Exposures (£k)	Past Due Exposures (£k)	Securitation Losses recognised in period (£k)
Originated Securitisations				
Credit Card Receivables (ABS)	-	-	-	-
Invested Securitisations				
Residential Mortgage Backed Securities (RMBS)	24,058	-	-	-
Residential Mortgage Backed Covered Bonds	21,026	-	-	-

Total Outstanding Securitisation Exposure as at 29 February 2012				
Securitisation Role / Exposure Type	Exposure Value (£k)	Impaired Exposures (£k)	Past Due Exposures (£k)	Securitation Losses recognised in period (£k)
Originated Securitisations				
Credit Card Receivables (ABS)	-	-	-	-
Invested Securitisations				
Residential Mortgage Backed Securities (RMBS)	45,423	-	-	-
Residential Mortgage Backed Covered Bonds	39,526	-	-	-

Originated securitisation transactions typically involve the sale of a group or portfolio of ring fenced loans to another entity, often known as a special purpose entity ('SPE'). For accounting purposes the SPE's are consolidated when the substance of the relationship indicates control. In assessing control all relevant quantitative and qualitative aspects are considered.

Invested positions are held as Available For Sale (AFS) assets on the Balance Sheet.

13.2. Risks inherent in Securitised and Covered Bond Assets

There are a number of inherent risks in purchasing certain securitised notes including the performance of the underlying assets, the explicit support of the Issuer and its financial stability and volatility in the market value of securitised notes.

The Company has established monitoring processes for investing in securitisation notes. It conducts reviews of Investor Reports by Issuers and an assessment is made of securitised asset performance (notably including arrears levels), operational risk, cash flow analysis, market prices / yields, legal analysis and counterparty risk at both programme and Issuer levels through quantitative and qualitative analysis.

The risks inherent in Covered Bonds relate primarily to the financial strength of the issuer and also to the underlying assets used as collateral for the bonds. A pre-purchase assessment of the Issuer's financial strength is undertaken together with an assessment of the bond structure and underlying assets, including areas such as arrears levels and collateral arrangements. An annual review of the Issuer's financial strength is undertaken.

13.3. Approach to Calculating Risk Weighted Exposure Amounts

The Company adopts the Standardised Approach in relation to all types of securitisation and covered bond exposures.

For invested positions the Company calculates risk weighted exposure amounts using the credit quality steps prescribed in BIPRU 9 for securitisations and BIPRU 3.4 for Covered Bond exposures. An approved ECAI is used for assessment of regulatory capital.

The following table details the Company's invested non-trading book securitisation and covered bond positions, capital resources requirements, credit quality steps and risk weight bands.

Securitisation Capital Resources Requirements

Total Outstanding as at 28 February 2013			
Credit Quality Step/Exposure Type	Exposure (£k)	Risk Weight (%)	Capital Resource Requirement (£k)
Credit Quality Step 1			
Residential Mortgage Backed Securities (RMBS)	24058	20%	385
Credit Quality Step 2			
Residential Mortgage Backed Covered Bond	21026	20%	336

Total Outstanding as at 29 February 2012			
Credit Quality Step/Exposure Type	Exposure (£k)	Risk Weight (%)	Capital Resource Requirement (£k)
Credit Quality Step 1			
Residential Mortgage Backed Securities (RMBS)	45423	20%	727
Credit Quality Step 2			
Residential Mortgage Backed Covered Bond	39526	20%	632

14. Remuneration

14.1. Remuneration Governance and Decision Making

The Bank has established a Remuneration Committee to oversee the determination of the Remuneration Policy ("the Policy") and decisions on reward for Code Staff. The Policy is reviewed on a regular basis by the Committee.

The Remuneration Committee's role is to determine remuneration policy for Code Staff, directly oversee remuneration arrangements for the senior directors within the Company's leadership team and all Code Staff, as well as colleagues in the key control functions of Risk, Compliance and Audit independently of other business areas.

The Remuneration Committee seeks to ensure that the levels and structures of remuneration are designed to attract, retain and motivate management talent needed to run the business in a way which is consistent with the risk appetite and on-going sustainability of the business and to be compliant with the applicable legislation and regulation.

The Committee is appointed by the Board and consists of three independent non-executive directors of the Company (one of whom is the Chairman of Tesco Bank). It met 4 times during 2012/13. The Committee is supported by the Personnel Director of Tesco Bank and a representative from the Tesco Plc Group Reward team. In addition, the Company's Chief Executive attends meetings at the request of the Committee. The Committee received independent advice from a number of external providers during the year, including Price Waterhouse Coopers, Mercer and Freshfield Bruckhaus Deringer LLP.

14.2. Aligning Performance and Reward –the link between pay and performance.

The overall aim of the Policy is to ensure an appropriate alignment between pay and total reward in line with the risk profile of the Company and it has set its risk appetite accordingly. At an operating level, the Company's risk appetite has been translated into Key Performance Indicators (KPIs) within the business, which build up into an overall assessment in the Company's steering wheel, the process for assessing a balanced scorecard as well as within its individual remuneration arrangements in a number of ways including:

- An appropriate combination of fixed and variable pay, benchmarked annually, ensuring the Company's fixed-variable ratios on remuneration are controlled and do not encourage inappropriate risk taking behaviour.
- Basing variable performance measures on a combination of balanced measures, including qualitative and quantitative factors. The use of the Company balanced scorecard as a way of assessing short-term performance is viewed as a balanced way of ensuring that stakeholders are considered as part of business performance (as opposed to solely financial measures) and that decisions are not taken for short-term financial gain to the detriment of other aspects of the business.
- Ensuring that all employees of the Company, including Code Staff, have a set of annual objectives and a clear personal development plan. Managers use objectives to communicate the required level of performance and to set expectations. They are a key part of how employee performance is managed. Performance development plans focus on the skills and behaviours appropriate to enable staff to do their jobs well and to help them fulfil their potential. An employee's progress is reviewed on a regular basis and every employee receives an annual performance rating. Individual objectives, performance reviews and personal development plans for Code Staff are shared with the Remuneration Committee as part of the process for determining variable award levels.
- The basis of assessment for the short-term bonus is adjusted for people in control functions, so greater emphasis is placed on the performance of the control function. The remuneration for Code Staff in key control functions are overseen by the Remuneration Committee.
- Maximum award levels are determined as percentages of salary, which are pre-set for the whole Company based on work level and individual performance rating. Awards are mathematically driven based on both business and personal performance. Weak individual performance – as identified through the annual ratings system – results in reduced or zero awards. Rewards are not increased over and above this calculation, and therefore the opportunity for an individual to benefit from increased rewards outside of this core structure does not exist.

- There is a strong share based element to the variable reward offered to support long-term commitment to sustainable performance, with all Code Staff subject to levels of deferral.
- All incentive awards include a claw back facility at the discretion of the Remuneration Committee.

The aggregate value of remuneration in 2012/13 was £9.9m, broken down as £4.8m to Senior Management * and £5.1m to other Code Staff.

* Senior management is defined as all senior directors operating within Work Level 5, non-executive directors and the Chairman of the Company. Other Code Staff includes directors at Work Level 4 and senior managers at Work Level 3 whose actions have a material impact on the risk profile of the Company.