

**GOLDMAN SACHS INTERNATIONAL BANK**

(unlimited company)

**STRATEGIC REPORT, DIRECTORS' REPORT AND FINANCIAL STATEMENTS**

**31 DECEMBER 2014**



# **GOLDMAN SACHS INTERNATIONAL BANK**

## **(unlimited company)**

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### **STRATEGIC REPORT**

The directors present their strategic report for the year ended 31 December 2014.

#### **1. Introduction**

Goldman Sachs International Bank ('the bank') acts as a primary dealer for European government bonds and is involved in bond trading, lending and deposit taking activities, and agency lending. The bank operates branches in Korea, (Goldman Sachs International Bank, Seoul Branch ('the Seoul branch')) which is involved in client execution activities, and Germany, (Goldman Sachs International Bank Zweigniederlassung Frankfurt ('the Frankfurt branch')) and has a representative office in China ('the Beijing rep office').

The bank's primary regulators are the Prudential Regulation Authority ('the PRA') and the Financial Conduct Authority ('the FCA').

The bank's ultimate parent undertaking and controlling entity is The Goldman Sachs Group, Inc. ('Group Inc.'). Group Inc. is a bank holding company and a financial holding company regulated by the Board of Governors of the Federal Reserve System ('Federal Reserve Board'). Group Inc. together with its consolidated subsidiaries form 'the group'. The group is a leading global investment banking, securities and investment management firm that provides a wide range of financial services to a substantial and diversified client base that includes corporations, financial institutions, governments and high-net-worth individuals.

As part of the group, the bank seeks to be a leading participant in the global financial markets in which it participates.

#### **2. Financial overview**

The financial statements have been drawn up for the year ended 31 December 2014 and comparative information has been presented for the year ended 31 December 2013.

The profit and loss account for the year ended 31 December 2014 is set out on page 12. Net interest expense decreased to US\$10 million for the year ended 31 December 2014 (year ended 31 December 2013: US\$21 million). This reflects the bank's continued focus on the diversification of funding sources, including the offering of certificates of deposits, and management of excess liquidity. The bank continues to expand its lending activities through lending to high-net-worth individuals.

Trading profit was US\$98 million for the year ended 31 December 2014 (year ended 31 December 2013: US\$166 million). The decrease reflects weaker performance in the bank's bond trading business, as macroeconomic uncertainty and low volatility led to challenging market-making conditions and generally lower levels of activity.

Administrative expenses of US\$76 million for the year ended 31 December 2014 (year ended 31 December 2013: US\$77 million) were essentially unchanged with the prior year.

The results for the bank show a profit on ordinary activities before taxation of US\$12 million for the year ended 31 December 2014 (year ended 31 December 2013: US\$68 million).

The balance sheet as at 31 December 2014 is set out on page 13. The bank had total assets of US\$44,070 million as at 31 December 2014 (31 December 2013: US\$47,627 million). The decrease was primarily attributable to a decrease in collateralised agreements with group undertakings as a result of lower market-making activity.

On 30 January 2015, to support growth in the bank's lending activities, the bank established a branch in Germany.

The bank primarily operates in a U.S. dollar environment as part of the group. Accordingly, the bank's functional currency is U.S. dollars and these financial statements have been prepared in that currency. The British pound / U.S. dollar exchange rate as at the balance sheet date was £ / US\$1.5579 (31 December 2013: £ / US\$1.6567). The average rate for the year was £ / US\$ 1.6455 (year ended 31 December 2013: £ / US\$ 1.5670).

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**STRATEGIC REPORT (continued)**

**2. Financial overview (continued)**

**Future outlook**

The directors consider that the year-end financial position of the bank was satisfactory. No significant change in the bank's principal business activity is expected.

**3. Business environment**

**Global**

During 2014, real gross domestic product ('GDP') growth appeared to improve in advanced economies and slow in emerging markets. Developed market growth improvements were largest in the United Kingdom and Euro area, while Japan's growth declined and the United States' growth improvement was modest. Monetary policy generally remained accommodative, helping most major advanced-economy equity markets to increase during the year, while longer-dated government bond yields generally declined. During the second half of 2014, the U.S. dollar strengthened and oil prices declined. Although macroeconomic conditions were fairly stable, U.S. equity market volatility increased towards the end of the year, alongside political uncertainty, particularly in Greece, Russia and the Middle East, as well as short-lived Ebola concerns. In emerging markets, headwinds from slowing domestic demand offset improving current account balances and contributed to a general slowdown in growth.

Unemployment rates in both the United States and United Kingdom declined in 2014 and at faster paces than in 2013. The Euro area unemployment rate declined in 2014, following an increase in 2013. The U.S. Federal Reserve ended its monthly asset purchase programme in the fourth quarter of 2014, after tapering its purchases for several months. The European Central Bank ('ECB') reduced its policy interest rate twice during the year, and along with the Bank of Japan, announced further easing policies. In investment banking, industry-wide underwriting activity remained strong in both equity and debt, and industry-wide completed mergers and acquisitions activity increased compared with 2013. Industry-wide announced mergers and acquisitions activity significantly increased compared with 2013.

**Europe**

In the Euro area, real GDP increased by 0.9% in 2014, compared with a contraction of 0.4% in 2013. While an improvement from 2013, growth remained at a suppressed level. Fixed investment and consumer spending both grew modestly in 2014, after contracting in 2013, and measures of inflation remain subdued. The ECB cut the main refinancing operations and deposit rates by 20 basis points to 0.05% and (0.20)%, respectively, announced a purchase programme for asset-backed securities and covered bonds in the fourth quarter of 2014, and discussed the possibility of a quantitative easing programme targeting sovereign bonds. The Euro depreciated by 12% against the U.S. dollar. In the United Kingdom, real GDP increased by 2.6% in 2014, compared with an increase of 1.7% in 2013. The Bank of England maintained its official bank rate at 0.50%. The British pound depreciated by 6% against the U.S. dollar. Yields on 10-year government bonds in the region generally fell during the year. In equity markets, the DAX Index and the Euro Stoxx 50 Index increased by 3% and 1%, respectively, while the FTSE 100 Index and the CAC 40 Index decreased by 3% and 1%, respectively, during 2014.

**Korea**

In Korea, real GDP increased by 3.3% showing continued signs of economic recovery. The Korean government cut the policy rate on two occasions by 25 basis points each. The Korean won depreciated by 4% against the U.S. dollar.

**4. Principal risks and uncertainties**

The bank faces a variety of risks that are substantial and inherent in its businesses including market, liquidity, credit, operational, legal, regulatory and reputational risks and uncertainties. The following are some of the more important factors that could affect the businesses.

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### **STRATEGIC REPORT (continued)**

#### **4. Principal risk and uncertainties (continued)**

##### **Economic and market conditions**

The bank's businesses, by their nature, do not produce predictable earnings and are materially affected by conditions in the global financial markets and economic conditions generally, both directly and through their impact on client activity. These conditions can change suddenly and very negatively.

##### **Regulation**

As a participant in the financial services industry and a subsidiary of a systemically important financial institution, the bank is subject to extensive regulation. The bank faces the risk of intervention by regulatory and taxing authorities in all jurisdictions in which it conducts its businesses. Among other things, as a result of regulators or private parties challenging the bank's compliance with enforcing existing laws and regulations, it could be fined, prohibited from engaging in some of its business activities, subject to limitations or conditions on its business activities or subjected to new or substantially higher taxes or other governmental charges in connection with the conduct of its businesses or with respect to its employees.

The bank may be adversely affected by increased governmental and regulatory scrutiny (from within the EU or other countries where it conducts business) or negative publicity. Governmental scrutiny from regulators, legislative bodies and law enforcement agencies with respect to matters relating to compensation, business practices, past actions and other matters has increased dramatically in the past several years. The financial crisis and the current political and public sentiment regarding financial institutions has resulted in a significant amount of adverse press coverage, as well as adverse statements or charges by regulators or other government officials. Press coverage and other public statements that assert some form of wrongdoing often result in some type of investigation by regulators, legislators and law enforcement officials or in lawsuits.

Responding to these investigations and lawsuits, regardless of the ultimate outcome of the proceeding, is time-consuming and expensive and can divert the time and effort of senior management from the bank's business. Penalties and fines sought by regulatory authorities have increased substantially over the last several years, and certain regulators have been more likely in recent years to commence enforcement actions or to advance or support legislation targeted at the financial services industry. Adverse publicity, governmental scrutiny and legal and enforcement proceedings can also have a negative impact on reputation and on the morale and performance of employees, which could adversely affect the bank's businesses and results of operations. In addition, the resolution of any civil, regulatory or criminal proceedings could have adverse consequences that include restrictions on the bank's current and future business activities.

There is also the risk that new laws or regulations or changes in enforcement of existing laws or regulations applicable to the bank's businesses or those of the bank's clients, including capital, liquidity, leverage and margin requirements, restrictions on leveraged lending or other business practices, reporting requirements, tax burdens and compensation restrictions, could be imposed on a limited subset of financial institutions (either based on size, activities, geography or other criteria), which may adversely affect the bank's ability to compete effectively with other institutions that are not affected in the same way. In addition, regulation imposed on financial institutions or market participants generally, such as taxes on financial transactions, could adversely impact levels of market activity more broadly, and thus impact the bank's businesses.

The EU and national financial legislators and regulators have proposed or adopted numerous market reforms that may impact the bank's businesses. These include stricter capital and liquidity requirements, including recently finalised legislation to implement Basel III capital requirements for the bank. These market reforms also include rules on the recovery and resolution of EU institutions, rules on the separation of certain trading activities from deposit taking, rules on the cross-border provision of services from countries outside the European Economic Area, authorisations for regulators to impose position limits, requirements to execute certain transactions only on certain regulated venues, reporting requirements (including requirements to publish information about transactions), restrictions on short selling and credit default swaps, sanctions for regulatory breach and further revised organisational, market structure, conduct of business and market abuse rules.

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### **STRATEGIC REPORT (continued)**

#### **4. Principal risk and uncertainties (continued)**

In addition, the European Commission, the European Securities Market Authority and the EBA have announced or are formulating regulatory standards and other measures which will impact the company's European operations. Certain GS Group entities, including the bank, are also regulated by the European securities, derivatives and commodities exchanges of which they are members. In February 2013, the European Commission published a proposal for enhanced cooperation in the area of financial transactions tax in response to a request from certain member states of the EU. The proposed financial transactions tax is broad in scope and would apply to transactions in a wide variety of financial instruments and derivatives. The draft legislation is still subject to further revisions and the full impact of the proposal will not be known with certainty until the legislation is finalised.

These developments could impact the bank's profitability in the affected jurisdictions, or even make it uneconomic to continue to conduct all or certain businesses in such jurisdictions, or could result in the bank incurring significant costs associated with changing business practices, restructuring businesses, moving certain businesses and employees to other locations or complying with applicable capital requirements, including liquidating assets or raising capital in a manner that adversely increases the bank's funding costs.

The bank is also subject to laws and regulations relating to the privacy of the information of clients, employees or others, and any failure to comply with these regulations could expose the bank to liability and / or reputational damage. In addition, the bank's businesses are increasingly subject to laws and regulations relating to surveillance, encryption and data on-shoring in the jurisdictions in which the company operates. Compliance with these laws and regulations may require the bank to change its policies, procedures and technology for information security (including cyber security), which could, among other things, make the bank more vulnerable to cyber-attacks and misappropriation, corruption or loss of information or technology.

#### **Market volatility**

Certain market-making activities depend on market volatility to provide trading and arbitrage opportunities to clients and decreases in volatility may reduce these opportunities and adversely affect the results of these activities. On the other hand, increased volatility, while it can increase trading volumes and spreads, also increases risk as measured by Value-at-Risk ('VaR') and may expose the bank to increased risks in connection with market-making activities or necessitate the reduction in size of these activities in order to avoid increasing VaR. Limiting the size of such market-making positions can adversely affect the bank's profitability. In periods when volatility is increasing, but asset values are declining significantly, it may not be possible to sell assets at all or it may only be possible to do so at steep discounts. In such circumstances, the bank may be forced to either take on additional risk or to incur losses in order to decrease its VaR. In addition, increases in volatility increase the level of the bank's risk-weighted assets ('RWAs'), which increases the bank's capital requirements.

#### **Liquidity**

Liquidity is essential to the bank's businesses. The bank's liquidity could be impaired by an inability to access secured and / or unsecured debt markets, an inability to access funds from Group Inc. or other affiliates, an inability to sell assets or redeem investments or unforeseen outflows of cash or collateral. This situation may arise due to circumstances that the bank may be unable to control, such as a general market disruption or an operational problem that affects third parties, the bank or its affiliates or even by the perception among market participants that the bank, or other market participants, are experiencing greater liquidity risk.

Furthermore, the bank's ability to sell assets may be impaired if other market participants are seeking to sell similar assets at the same time, as is likely to occur in a liquidity or other market crisis or in response to changes to rules or regulations. In addition, financial institutions with which the bank interacts may exercise set off rights or the right to require additional collateral, including in difficult market conditions, which could further impair the bank's access to liquidity.

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**STRATEGIC REPORT (continued)**

**4. Principal risk and uncertainties (continued)**

**Credit risk**

The bank is exposed to the risk that third parties who owe money, securities or other assets will not perform their obligations. These parties may default on their obligations to the bank due to bankruptcy, lack of liquidity, operational failure or other reasons. A failure of a significant market participant, or even concerns about a default by such an institution, could lead to significant liquidity problems, losses or defaults by other institutions, which in turn could adversely affect the bank.

The bank is also subject to the risk that its rights against third parties may not be enforceable in all circumstances. In addition, deterioration in the credit quality of third parties whose securities or obligations are held by the bank including a deterioration in the value of collateral posted by third parties to secure their obligations to the bank under derivatives contracts and loan agreements, could result in losses and / or adversely affect the bank's ability to rehypothecate or otherwise use those securities or obligations for liquidity purposes.

A significant downgrade in the credit ratings of the bank's counterparties could also have a negative impact on the bank's results. While, in many cases, the bank is permitted to require additional collateral from counterparties that experience financial difficulty, disputes may arise as to the amount of collateral the bank is entitled to receive and the value of pledged assets. The termination of contracts and the foreclosure on collateral may subject the bank to claims for the improper exercise of its rights. Default rates, downgrades and disputes with counterparties as to the valuation of collateral increase significantly in times of market stress and illiquidity.

**Derivative transactions**

The bank is party to a large number of derivative transactions. Many of these derivative instruments are individually negotiated and non-standardised, which can make exiting, transferring or settling positions difficult.

Derivative transactions may also involve the risk that documentation has not been properly executed, that executed agreements may not be enforceable against the counterparty, or that obligations under such agreements may not be able to be netted against other obligations with such counterparty. In addition, counterparties may claim that such transactions were not appropriate or authorised.

Derivative contracts and other transactions entered into with third parties are not always confirmed by the counterparties or settled on a timely basis. While the transaction remains unconfirmed or during any delay in settlement, the bank is subject to heightened credit and operational risk and in the event of a default may find it more difficult to enforce its rights. In addition, as new complex derivative products are created, disputes about the terms of the underlying contracts could arise, which could impair the bank's ability to effectively manage its risk exposures from these products and subject the bank to increased costs. The provisions of legislation requiring central clearing of OTC derivatives, or a market shift toward standardised derivatives, could reduce the risk associated with such transactions, but under certain circumstances could also limit the bank's ability to develop derivatives that best suit the needs of clients and to hedge its own risks, and could adversely affect the bank's profitability and increase credit exposure to such platform.

**Operational infrastructure**

The bank's businesses are highly dependent on its ability to process and monitor, on a daily basis, a very large number of transactions, many of which are highly complex, and occur at very high volumes and frequencies, across numerous and diverse markets in many currencies. These transactions, as well as information technology services provided to clients, often must adhere to client-specific guidelines, as well as legal and regulatory standards.

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### **STRATEGIC REPORT (continued)**

#### **4. Principal risk and uncertainties (continued)**

As the bank's client base and geographical reach expands, and the volume, speed, frequency and complexity of transactions, especially electronic transactions (as well as the requirements to report such transactions on a real-time basis to clients, regulators and exchanges) increases, developing and maintaining operational systems and infrastructure becomes more challenging, and the risk of systems or human error in connection with such transactions increases, as well as the potential consequences of such errors due to the speed and volume of transactions involved and the potential difficulty associated with discovering such errors quickly enough to limit the resulting consequences.

Financial, accounting, data processing or other operating systems and facilities may fail to operate properly or become disabled as a result of events that are wholly or partially beyond the bank's control, such as a spike in transaction volume, adversely affecting the ability to process these transactions or provide these services. The bank must continuously update these systems to support its operations and growth and to respond to changes in regulations and markets, and invest heavily in systemic controls and training to ensure that such transactions do not violate applicable rules and regulations or, due to errors in processing such transactions, adversely affect markets, clients and counterparties or the bank itself.

The bank also faces the risk of operational failure, termination or capacity constraints of any of the clearing agents, exchanges, clearing houses or other financial intermediaries that it uses to facilitate securities and derivatives transactions and, as interconnectivity with clients grows, the bank will increasingly face the risk of operational failure with respect to clients' systems. Any such failure, termination or constraint could adversely affect the bank's ability to effect transactions, service its clients and manage its exposure to risk.

Despite the resiliency plans and facilities that are in place, the bank's ability to conduct business may be adversely impacted by a disruption in the infrastructure that supports these businesses and the communities in which the bank is located. This may include a disruption involving electrical, communications, internet, transportation or other services facilities used by the bank or third parties with which the bank conducts business.

#### **Technology**

Technology is fundamental to the bank's businesses and industry. The growth of electronic trading and the introduction of new technologies is changing these businesses and presenting the bank with new challenges. Securities, futures and options transactions are increasingly occurring electronically, both on the bank's own systems and through other alternative trading systems, and it appears that the trend toward alternative trading systems will continue and probably accelerate. Some of these alternative trading systems compete with the bank's businesses increasing competitive pressures in these and other areas. In addition, the increased use by clients of low-cost electronic trading systems and direct electronic access to trading markets could cause a reduction in commissions and spreads. As clients increasingly use the bank's systems to trade directly in the markets, the bank may incur liabilities as a result of their use of its order routing and execution infrastructure. Significant resources have been invested into the development of electronic trading systems and the bank expects to continue to do so, but there is no assurance that the revenues generated by these systems will yield an adequate return on this investment, particularly given the relatively lower commissions arising from electronic trades.

#### **Risk management**

The bank seeks to monitor and control risk exposure through a risk and control framework encompassing a variety of separate, but complementary financial, credit, operational, compliance and legal reporting systems, internal controls, management review processes and other mechanisms. The risk management process seeks to balance the bank's ability to profit from market-making positions with exposure to potential losses. Whilst the bank employs a broad and diversified set of risk monitoring and risk mitigation techniques, those techniques and the judgements that accompany their application cannot anticipate every economic and financial outcome or the specifics and timing of such outcomes. Thus, the bank may, in the course of its activities, incur losses.

In addition, refer to the financial risk management section in note 23 to the financial statements.

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**STRATEGIC REPORT (continued)**

**5. Credit ratings**

The table below presents the unsecured credit ratings of the bank as at 31 December 2014.

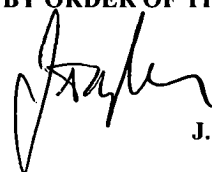
	<b>Standard &amp; Poor's Rating Services</b>	<b>Moody's Investors Service</b>	<b>Fitch Ratings, Inc.</b>
Short-term deposit	-	P-1	F1
Short-term debt	A-1	P-1	F1
Long-term deposit	-	A2	A
Long-term debt	A	A2	A
Ratings outlook	Stable	Stable <sup>1</sup>	Stable

1. On 17 March 2015, Moody's Investors Service placed the long-term debt ratings of the bank under review for upgrade following the publication of its new bank rating methodology.

**6. Date of authorisation of issue**

The strategic report was authorised for issue by the Board of Directors on 23 April 2015.

**BY ORDER OF THE BOARD**



**J. P. Herman**

**Secretary**

**23 April 2015**

**GOLDMAN SACHS INTERNATIONAL BANK**  
**(unlimited company)**

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**REPORT OF THE DIRECTORS**

The directors present their report and audited financial statements for the year ended 31 December 2014.

**1. Introduction**

In accordance with section 414A of the Companies Act 2006, the directors have prepared a strategic report, which contains a review of the bank's businesses and a description of the principal risks and uncertainties facing the bank. The directors have chosen to make reference to the bank's risk management objectives and policies, including exposures to market risk, credit risk and liquidity risk, and the future outlook of the bank in the strategic report in accordance with section 414C(11) of the Companies Act 2006.

**2. Dividends**

The directors do not recommend the payment of an ordinary dividend in respect of the year (year ended 31 December 2013: US\$nil).

**3. Employment of disabled persons**

Applications for employment by disabled persons are fully and fairly considered having regard to the aptitudes and abilities of each applicant. Efforts are made to enable any employees who become disabled during employment to continue their careers within the group. Training, career development and promotion of disabled persons are, to the extent possible, identical to that of other employees who are not disabled.

**4. Employee involvement**

It is group policy that there should be effective communication with all employees who, subject to practical and commercial considerations, should be consulted on and involved in decisions that affect their current jobs or future prospects. Employees share in performance-based incentive schemes.

**5. Directors**

The directors of the bank who served throughout the year and to the date of this report were:

**Name**

E. G. Corrigan, Chairman  
Lord Griffiths of Fforestfach  
E. H. Leouzon  
D. W. McDonogh  
D. G. J. Paterson  
E. E. Stecher  
R. A. Vince  
D. D. Wildermuth

No director had, at the year end, any interest requiring note herein.

**6. Financial risk management**

The bank's risk management objectives and policies, as well as exposures to market, credit, liquidity and other risks are described in the strategic report and note 23 to the financial statements.

**7. Disclosure of information to auditors**

In the case of each of the persons who are directors of the bank at the date when this report was approved:

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**REPORT OF THE DIRECTORS (continued)**

**7. Disclosure of information to auditors (continued)**

- So far as each of the directors is aware, there is no relevant audit information of which the bank's auditors are unaware; and
- Each of the directors has taken all the steps that he / she ought to have taken as a director to make himself / herself aware of any relevant audit information and to establish that the bank's auditors are aware of that information.

**8. Independent auditors**

Prior to 1 October 2007, the bank passed an elective resolution under section 386 of the Companies Act 1985 to dispense with the annual reappointment of auditors. PricewaterhouseCoopers LLP will, accordingly, continue in office as auditors of the bank pursuant to section 487(2) of the Companies Act 2006 and paragraph 44 of schedule 3 to the Companies Act 2006 (Commencement No. 3 Consequential Amendment, Transitional Provisions and Savings) Order 2007.

**9. Statement of directors' responsibilities**

The directors are responsible for preparing the strategic report, the directors' report and the financial statements in accordance with applicable law and regulations. Company law requires the directors to prepare accounts for each financial period which give a true and fair view of the state of affairs of the bank as at the end of the financial period and of the profit or loss of the bank for that period. In preparing those accounts, the directors are required to:

- Select suitable accounting policies and then apply them consistently;
- Make judgements and estimates that are reasonable and prudent;
- State whether applicable accounting standards have been followed subject to any material departures disclosed and explained in the financial statements; and
- Prepare the accounts on the going concern basis unless it is inappropriate to presume that the bank will continue in business.

The directors are responsible for keeping adequate accounting records which disclose with reasonable accuracy at any time the financial position of the bank and to enable them to ensure that the accounts comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the bank and, hence, for taking reasonable steps for the prevention and detection of fraud and other irregularities.

**10. Date of authorisation of issue**

The financial statements were authorised for issue by the Board of Directors on 23 April 2015.

**BY ORDER OF THE BOARD**



**J. P. Herman**

**Secretary**

**23 April 2015**

# **Independent auditors' report to the members of Goldman Sachs International Bank (unlimited company)**

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## **Report on the financial statements**

### **Our opinion**

In our opinion, Goldman Sachs International Bank's financial statements ("the financial statements"):

- give a true and fair view of the state of the bank's affairs as at 31 December 2014 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

### **What we have audited**

Goldman Sachs International Bank's financial statements comprise:

- the balance sheet as at 31 December 2014;
- the profit and loss account and statement of total recognised gains and losses for the year then ended; and
- the notes to the financial statements, which include a summary of significant accounting policies and other explanatory information.

The financial reporting framework that has been applied in the preparation of the financial statements is applicable law and United Kingdom Accounting Standards (United Kingdom Generally Accepted Accounting Practice).

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

### **Opinion on other matter prescribed by the Companies Act 2006**

In our opinion, the information given in the strategic report and directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements.

### **Other matters on which we are required to report by exception**

#### **Adequacy of accounting records and information and explanations received**

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

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

We have no exceptions to report arising from this responsibility.

### **Directors' remuneration**

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

### **Responsibilities for the financial statements and the audit**

#### **Our responsibilities and those of the directors**

As explained more fully in the statement of directors' responsibilities set out on page 9, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

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

**Independent auditors' report to the members of  
Goldman Sachs International Bank  
(unlimited company)**

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

**What an audit of financial statements involves**

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

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

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

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

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

Duncan McNab (Senior Statutory Auditor)  
for and on behalf of PricewaterhouseCoopers LLP  
Chartered Accountants and Statutory Auditors  
7 More London Riverside  
London  
SE1 2RT  
24 April 2015

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**PROFIT AND LOSS ACCOUNT**

**for the year ended 31 December 2014**

		Year Ended 31 December 2014	Year Ended 31 December 2013
	Note	US\$'000	US\$'000
Interest receivable and similar income	4	77,953	65,021
Interest payable and similar charges	5	(88,378)	(86,065)
Net interest expense		(10,425)	(21,044)
Trading profit	3	98,315	166,050
<b>TOTAL OPERATING INCOME</b>		<b>87,890</b>	<b>145,006</b>
Administrative expenses		(75,636)	(76,666)
<b>PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION</b>	6	<b>12,254</b>	<b>68,340</b>
Tax on profit on ordinary activities	10	(310)	(16,936)
<b>PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION AND FOR THE FINANCIAL YEAR</b>	21	<b>11,944</b>	<b>51,404</b>

Total operating income and profit on ordinary activities before taxation of the bank are derived from continuing operations in the current and prior years.

**STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES**

**for the year ended 31 December 2014**

		Year Ended 31 December 2014	Year Ended 31 December 2013
	Note	US\$'000	US\$'000
Profit for the financial year		11,944	51,404
Translation (loss) / gain	21	(8,674)	3,974
Gain / (loss) on net investment hedge	21	4,246	(6,401)
<b>TOTAL RECOGNISED GAINS AND LOSSES RELATING TO THE FINANCIAL YEAR AND SINCE LAST FINANCIAL STATEMENTS</b>		<b>7,516</b>	<b>48,977</b>

The notes on pages 14 to 44 form an integral part of these financial statements.  
Independent auditors' report – pages 10 to 11.

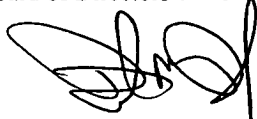
**GOLDMAN SACHS INTERNATIONAL BANK**  
**(unlimited company)**

**BALANCE SHEET**

**as at 31 December 2014**

	Note	31 December 2014 US\$'000	31 December 2013 US\$'000
<b>ASSETS</b>			
Cash at bank and in hand		115,919	128,808
Customer accounts receivable	11	3,309,526	5,302,257
Financial instruments owned	12	9,957,994	7,014,452
Financial instruments owned pledged as collateral	12	7,234,608	9,234,763
Collateralised agreements with group undertakings	13	22,709,036	25,929,110
Tangible fixed assets	14	727	641
Other assets	15	742,004	17,464
<b>Total assets</b>		<b>44,069,814</b>	<b>47,627,495</b>
<b>LIABILITIES AND SHAREHOLDER'S FUNDS</b>			
Customer accounts payable	17	13,851,605	11,903,565
Deposits by banks		3,292,680	2,528,745
Financial instruments sold, but not yet purchased	12	12,974,774	16,368,273
Collateralised financing with group undertakings		8,976,919	11,926,181
Other liabilities	18	1,544,823	1,479,234
Long-term subordinated loans from group undertakings	19	826,182	826,182
<b>Total liabilities</b>		<b>41,466,983</b>	<b>45,032,180</b>
Called up share capital	20	62,558	62,558
Share premium account	21	2,094,303	2,094,303
Other reserve account	21	(19,577)	(15,149)
Profit and loss account	21	465,547	453,603
<b>Total shareholder's funds</b>	21	<b>2,602,831</b>	<b>2,595,315</b>
<b>Total liabilities and shareholder's funds</b>		<b>44,069,814</b>	<b>47,627,495</b>
<b>MEMORANDUM ITEMS</b>			
Commitments	22	4,680,615	1,634,053
Contingent liabilities	22	2,415,156	1,898,801

The financial statements were approved by the Board of Directors on 23 April 2015 and signed on its behalf by:



D. W. McDonogh  
Director

The notes on pages 14 to 44 form an integral part of these financial statements.  
Independent auditors' report – pages 10 to 11.  
Company number: 1122503

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES**

**a. Accounting convention**

The financial statements have been prepared on the going concern basis, under the historical cost convention (modified as explained in *note 11*), and in accordance with the Companies Act 2006 and applicable accounting standards in the United Kingdom. The principal accounting policies are set out below and have been applied consistently throughout the year.

**b. Revenue recognition**

Trading profit, which is after charging related expenses, comprises revenues from bond trading, client execution activities, lending and deposit taking activities, and agency lending. Related expenses include trading interest payable, trading interest receivable and related financing transactions.

Financial assets and financial liabilities held for trading or designated at fair value through profit or loss are recognised at fair value with realised and unrealised gains and losses as well as associated interest and expenses included in total operating income. Financial assets are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs.

Finance revenue on loans and receivables is recorded in interest receivable and similar income using the effective interest method.

Commission revenues from agency lending are recognised on the day the trade is executed.

**c. Operating leases**

The bank has entered into operating lease arrangements as the lessee. Leased assets are not recognised on the balance sheet. Costs in respect of operating leases, adjusted for any incentives granted by the lessor, are charged on a straight-line basis over the lease term and included within administrative expenses in the profit and loss account.

**d. Short-term employee benefits**

Short-term employee benefits, such as wages and salaries, are measured on an undiscounted basis and accrued as an expense over the period in which the employee renders the service to the bank. Provision is made for discretionary year end compensation whether to be paid in cash or share-based awards where, as a result of bank policy and past practice, a constructive obligation exists at the balance sheet date.

**e. Share-based payments**

Group Inc. issues awards in the form of restricted stock units ('RSUs') and stock options to the bank's employees for services rendered to the bank. Awards are classified as equity settled and hence the cost of share-based transactions with employees is measured based on the grant-date fair value of the award. Share-based awards that do not require future service (i.e. vested awards, including awards granted to retirement eligible employees) are expensed immediately. Share-based awards that require future service are amortised over the relevant service period. Expected forfeitures are included in determining share-based employee compensation expense.

Group Inc. settles equity awards through the delivery of its ordinary shares. Group Inc. pays cash dividend equivalents on outstanding RSUs. The bank has also entered into a chargeback agreement with Group Inc. under which it is committed to pay to Group Inc. the grant-date fair value as well as subsequent movements in fair value of those awards to Group Inc. at the time of delivery to its employees.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**f. Foreign currencies**

Transactions denominated in foreign currencies are translated into U.S. dollars at rates of exchange ruling on the date the transaction occurred. Monetary assets and liabilities denominated in foreign currencies are translated into U.S. dollars at rates of exchange ruling at the balance sheet date. Foreign exchange gains and losses are recognised in administrative expenses.

The results of branches and representative offices with non-U.S. dollar functional currencies are translated at the average rates of exchange during the year and their balance sheets at the rates ruling at the balance sheet date. Exchange differences arising from the retranslation of the opening net assets and results are reported in the statement of total recognised gains and losses.

**g. Net investment hedging**

Where net investment hedging is employed, all gains and losses on the effective portion of the hedging instrument, together with any gains and losses on the foreign currency translation of the hedge investment, are taken directly to the statement of total recognised gains and losses. Any gains or losses on the ineffective portion are recognised immediately in the profit and loss account. The cumulative gains and losses on the hedging instrument and gains and losses on the translation of the hedged investment are recognised in the profit and loss account only on disposal of the investment.

**h. Dividends**

Final equity dividends are recognised as a liability and deducted from equity in the period in which the dividends are approved by the bank's shareholder. Interim equity dividends are recognised and deducted from equity when paid.

**i. Pension costs**

The bank sponsors a defined contribution plan. The contributions payable for the year are charged to administrative expenses. Differences between contributions payable for the year and contributions actually paid are shown as either accruals or prepayments on the balance sheet.

**j. Tangible fixed assets**

Tangible fixed assets are stated at cost less accumulated depreciation and provision for any impairment. Depreciation is included in administrative expenses and is provided on a straight-line basis over the following estimated useful lives:

	<u>Years</u>
Fixtures, fittings & equipment	3-7

Leasehold improvements are depreciated over the shorter of the useful economic life of the asset or the remaining life of the lease when the asset is brought into use. Depreciation policies are reviewed on an annual basis.

**k. Cash at bank and in hand**

Cash at bank and in hand is highly liquid overnight deposits held in the ordinary course of business.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**i. Financial instruments**

**i. Recognition and derecognition**

Financial assets and financial liabilities are recognised when the bank becomes party to the contractual provisions of the instrument. The regular way purchase and sale of cash inventory is recognised and derecognised using trade date accounting.

The bank derecognises financial assets when the contractual right to the cash flows from the financial asset expire or if it transfers the financial asset and substantially all the risk and rewards of ownership of that financial asset. A financial liability is derecognised only when it is extinguished (i.e. when the obligation specified in the contract is discharged or cancelled or expires).

**ii. Classification and measurement**

The bank classifies its financial instruments into the below categories. The classification depends on the purpose for which the financial instruments were acquired or originated. The bank determines the classification of its financial instruments at initial recognition.

**Financial instruments classified as held for trading**

Financial instruments classified as held for trading include financial instruments owned and financial instruments sold, but not yet purchased. This includes derivative and cash instruments. Financial instruments classified as held for trading are initially recognised at fair value with transaction costs expensed in profit or loss. Such financial instruments are carried in the balance sheet at fair value and all subsequent gains or losses are recognised in trading profit. See iv. *fair value measurement* below for further information on the measurement of financial instruments classified as held for trading.

The directors are of the opinion that it would not be appropriate to classify them as current asset investments or to provide an analysis of such securities between those listed and unlisted.

**Financial instruments designated at fair value through profit or loss**

The bank designates certain of its other financial assets and financial liabilities at fair value through profit or loss. Financial instruments designated at fair value through profit or loss are initially recognised at fair value with transaction costs expensed in profit or loss. Such financial instruments are carried in the balance sheet at fair value and all subsequent gains or losses are recognised in total operating income. The primary reasons for designating such financial assets and financial liabilities at fair value through profit or loss are:

- The group of financial assets, financial liabilities or both is managed and its performance evaluated on a fair value basis; and
- To eliminate or significantly reduce a measurement or recognition inconsistency that would otherwise arise from measuring assets or liabilities or recognised the gains and losses on them on different bases.

Other financial assets and financial liabilities designated at fair value through profit or loss include:

- Resale agreements, other secured lending arrangements and repurchase agreements; and
- Certain customer accounts payable and all deposits by banks.

**GOLDMAN SACHS INTERNATIONAL BANK**  
**(unlimited company)**

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**I. Financial instruments (continued)**

These financial assets and financial liabilities at fair value are generally valued based on discounted cash flow techniques, which incorporate inputs with reasonable levels of price transparency, and are generally classified as level 2 (refer to *iv. fair value measurements*) because the inputs are observable. Valuation adjustments may be made for liquidity and for counterparty and group's credit quality.

**Loans and receivables; and financial liabilities measured at amortised cost**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. They include all cash at bank and in hand, customer accounts receivable and other assets. Such financial assets are initially measured at fair value plus transaction costs and are subsequently measured at amortised cost using the effective interest method (see below). Finance revenue is recorded in interest receivable and similar income.

Financial liabilities measured at amortised cost include certain customer accounts payable, all other liabilities and subordinated loans. Such financial liabilities are initially recognised at fair value plus transaction costs and subsequently measured at amortised cost using the effective interest method (see below). Finance costs, including discounts allowed on issue, are recorded in interest payable and similar charges.

The effective interest method is a method of calculating the amortised cost of a financial asset or a financial liability (or a group of financial assets or financial liabilities) and of allocating the interest income or interest expense over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments or receipts through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the bank estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all fees and points paid or received that are an integral part of the effective interest rate, transaction costs, and all other premiums or discounts.

The bank assesses its financial assets at each balance sheet date for any objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the financial asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The amount of the loss is included within administrative expenses.

**iii. Offsetting financial assets and financial liabilities**

Financial assets and financial liabilities are offset and the net amount presented in the balance sheet where there is:

- Currently a legally enforceable right to set off the recognised amounts; and
- Intent to settle on a net basis or to realise the asset and settle the liability simultaneously.

Where these conditions are not met, financial assets and financial liabilities are presented on a gross basis on the balance sheet.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**I. Financial instruments (continued)**

**iv. Fair value measurements**

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e. the exit price. Financial assets are marked to bid prices and financial liabilities are marked to offer prices. Fair value measurements do not include transaction costs. Fair value gains or losses are included in trading profit. Certain financial assets and financial liabilities are measured as a portfolio (i.e. based on its net exposure to market and / or credit risks).

The best evidence of fair value is a quoted price in an active market. If quoted prices in active markets are not available, fair value is determined by reference to prices for similar instruments, quoted prices or recent transactions in less active markets, or internally developed models that primarily use market-based or independently sourced parameters as inputs including, but not limited to, interest rates, volatilities, equity or debt prices, foreign exchange rates, credit spreads and funding spreads (i.e. the spread, or difference, between the interest rate at which a borrower could finance a given financial instrument relative to a benchmark interest rate).

United Kingdom Generally Accepted Accounting Practice has a three-level fair value hierarchy for disclosure of fair value measurements. The fair value hierarchy prioritises inputs to the valuation techniques used to measure fair value, giving the highest priority to level 1 inputs and the lowest priority to level 3 inputs. A financial instrument's level in the fair value hierarchy is based on the lowest level of input that is significant to its fair value measurement. The fair value hierarchy is as follows:

**Level 1.** Inputs are unadjusted quoted prices in active markets to which the bank had access at the measurement date for identical, unrestricted assets or liabilities.

**Level 2.** Inputs to valuation techniques are observable, either directly or indirectly.

**Level 3.** One or more inputs to valuation techniques are significant and unobservable.

Certain level 2 and level 3 financial assets and financial liabilities may require appropriate valuation adjustments that a market participant would require to arrive at fair value for factors such as counterparty and group's credit quality, funding risk, transfer restrictions, illiquidity and bid / offer spreads. Valuation adjustments are generally based on market evidence.

**Cash instruments**

Cash instruments include government bonds and bank loans. Valuation techniques and significant inputs for each level of the fair value hierarchy include:

- Level 1 cash instruments that are valued using quoted prices for identical unrestricted instruments in active markets.
- Level 2 cash instruments that are valued by verifying to quoted prices, recent trading activity for identical or similar instruments, broker or dealer quotations or alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations (e.g. indicative or firm) and the relationship of recent market activity to the prices provided from alternative pricing sources.

Valuation adjustments are typically made to level 2 cash instruments (i) if the cash instrument is subject to transfer restrictions and / or (ii) for other premiums and discounts that a market participant would require to arrive at fair value. Valuation adjustments are generally based on market evidence.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**1. Financial instruments (continued)**

- Level 3 cash instruments that have one or more significant valuation inputs that are not observable. Absent evidence to the contrary, level 3 cash instruments are initially valued at transaction price, which is considered to be the best initial estimate of fair value. Subsequently, the bank uses other methodologies to determine fair value, which vary based on the type of instrument. Valuation inputs and assumptions are changed when corroborated by substantive observable evidence, including values realised on sales of financial assets.

**Derivatives**

Derivatives may be traded on an exchange ('exchange-traded') or they may be privately negotiated contracts, which are usually referred to as OTC derivatives. Certain of the bank's OTC derivatives are cleared and settled through central clearing counterparties ('OTC-cleared'), while others are bilateral contracts between two counterparties ('bilateral OTC'). Valuation techniques and significant inputs for each level of the fair value hierarchy include:

- Level 1 derivatives include short-term contracts for future delivery of securities when the underlying security is a level 1 instrument, and exchange-traded derivatives if they are actively traded and are valued at their quoted market price.
- Level 2 derivatives include OTC derivatives for which all significant valuation inputs are corroborated by market evidence and exchange-traded derivatives that are not actively traded and / or that are valued using models that calibrate to market-clearing levels of OTC derivatives. In evaluating the significance of a valuation input, the bank considers, among other factors, a portfolio's net risk exposure to that input.

The selection of a particular model to value an OTC derivative depends on the contractual terms of and specific risks inherent in the instrument, as well as the availability of pricing information in the market. For derivatives that trade in liquid markets, model selection does not involve significant management judgement because outputs of models can be calibrated to market-clearing levels.

Valuation models require a variety of inputs, such as contractual terms, market prices, yield curves, discount rates (including those derived from interest rates on collateral received and posted as specified in credit support agreements for collateralised derivatives), credit curves, measures of volatility, prepayment rates, loss severity rates and correlations of such inputs. Significant inputs to the valuations of level 2 derivatives can be verified to market transactions, broker or dealer quotations or other alternative pricing sources with reasonable levels of price transparency. Consideration is given to the nature of the quotations (e.g. indicative or firm) and the relationship of recent market activity to the prices provided from alternative pricing sources.

- Level 3 derivatives are valued using models which utilise observable level 1 and / or level 2 inputs, as well as unobservable level 3 inputs. Unobservable inputs include certain correlations as well as credit spreads and equity volatility inputs.

Subsequent to the initial valuation of a level 3 derivative, the bank updates the level 1 and level 2 inputs to reflect observable market changes and any resulting gains and losses are recorded in level 3. Level 3 inputs are changed when corroborated by evidence such as similar market transactions, third-party pricing services and / or broker or dealer quotations or other empirical market data. In circumstances where the bank cannot verify the model value by reference to market transactions, it is possible that a different valuation model could produce a materially different estimate of fair value.

Where there is a difference between the initial transaction price and the fair value calculated by internal models, a gain or loss shall be recognised after initial recognition only to the extent that it arises from a change in a factor (including time) that market participants would consider in setting a price.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**l. Financial instruments (continued)**

**v. Hedge accounting**

The bank applies hedge accounting for certain interest rate swaps used to manage the interest rate exposure of certain fixed-rate customer deposits. To qualify for hedge accounting, the derivative hedge must be highly effective at reducing the risk from the exposure being hedged. Additionally, the bank must formally document the hedging relationship at inception and test the hedging relationship to ensure the derivative hedge continues to be highly effective over the life of the hedging relationship.

**m. Collateralised agreements and financing**

Collateralised agreements are resale agreements and other secured lending arrangements. Collateralised financing are repurchase agreements. Refer to *l. financial instruments*, above, for further information on the classification and measurement of these financial instruments. Collateral received or posted can be in the form of cash or securities. Cash collateral is recognised / derecognised when received / paid. Collateral posted by the bank in the form of securities is not derecognised from the balance sheet, whilst collateral received in the form of securities is not recognised on the balance sheet. If collateral received is subsequently sold, the obligation to return the collateral and the cash received are recognised on balance sheet.

**n. Current and deferred taxation**

The tax expense for the period comprises current and deferred taxation. Tax is recognised in the profit and loss account.

Current tax is calculated on the basis of the tax laws enacted or substantively enacted at the balance sheet date in the countries where the bank operates and generates taxable income.

Deferred tax is recognised in respect of all timing differences that have originated, but not reversed at the balance sheet date, where transactions or events have occurred at that date that will result in an obligation to pay more tax or a right to pay less tax in the future with the following exceptions:

- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.
- Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

**o. Provisions and contingent liabilities**

Provisions are recognised in the financial statements when it is probable that an outflow of economic benefits will be required to settle a present (legal or constructive) obligation, which has arisen as a result of past events, and for which a reliable estimate can be made of the amount of the obligation. Legal obligations that may arise as a result of proposed new laws are recognised as obligations only when the legislation is virtually certain to be enacted as drafted.

Contingent liabilities are:

- Possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events outside the control of the bank; or

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**1. ACCOUNTING POLICIES (continued)**

**o. Provisions and contingent liabilities (continued)**

- Present obligations that have arisen from past events but which are not recognised because either an outflow of economic benefits is not probable or the amount of the obligations cannot be reliably measured.

Contingent liabilities are not recognised in the financial statements. However, disclosure is made unless the probability of settlement is remote.

**2. REPORTING AND DISCLOSURE EXEMPTIONS**

**a. FRS1 (Revised 1996) 'Cash Flow Statements'**

The bank is a greater than 90% subsidiary of Group Inc. whose consolidated financial statements include the bank and are publicly available and is, therefore, exempt from preparing a cash flow statement as required by FRS1 (Revised 1996) 'Cash Flow Statements'.

**b. FRS8 'Related Party Disclosures'**

The bank is a wholly-owned subsidiary of Group Inc. whose consolidated financial statements include the bank and are publicly available. As a result, under the terms of paragraph 3(c) of FRS8 'Related Party Disclosures', the bank is exempt from disclosing transactions with companies also wholly owned within Group, Inc. There were no other related party transactions requiring disclosure.

**3. SEGMENTAL REPORTING**

The bank operates in two geographically distinct regions, Europe, Middle East and Africa ('EMEA'), the location of the head office, and Asia, the location of the Seoul branch and the Beijing rep office. Geographic segmental analysis is provided below. Geographic results have been allocated between EMEA and Asia based on the location of the business.

	<b>EMEA</b>		<b>Asia</b>		<b>Total</b>	
	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>	<b>2014</b>	<b>2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
Trading profit	86,561	141,973	11,754	24,077	98,315	166,050
Profit / (loss) on ordinary activities before taxation	13,263	60,546	(1,009)	7,794	12,254	68,340
Net assets	2,305,468	2,318,908	297,363	276,407	2,602,831	2,595,315

The bank reports its business segments in line with that of the group:

- Investment Banking - comprises underwriting and origination of debt instruments including government bonds and bank loans;
- Institutional Client Services - comprises client execution activities, market-making in European government bonds, interest rate products and currencies, secondary dealing in bank loans and agency lending; and
- Investing & Lending - comprises investment activities across various asset classes, primarily bank loans, which are typically longer-term.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**3. SEGMENTAL REPORTING (continued)**

The bank's trading profit is categorised into the following business segments:

	Year Ended 31 December 2014	Year Ended 31 December 2013
	US\$'000	US\$'000
Investment Banking	22,569	14,758
Institutional Client Services	66,857	128,330
Investing & Lending	8,889	22,962
	<b>98,315</b>	<b>166,050</b>

The bank has reclassified US\$7 million of trading profit for 2013 from Institutional Client Services to Investing & Lending associated with longer-term bank loan activity. There is no impact to total trading profit.

**4. INTEREST RECEIVABLE AND SIMILAR INCOME**

	Year Ended 31 December 2014	Year Ended 31 December 2013
	US\$'000	US\$'000
Interest on loans to banks and customers	3,979	7,152
Interest on collateralised agreements with group undertakings	65,144	57,842
Interest on loans to group undertakings	8,830	27
	<b>77,953</b>	<b>65,021</b>

**5. INTEREST PAYABLE AND SIMILAR CHARGES**

	Year Ended 31 December 2014	Year Ended 31 December 2013
	US\$'000	US\$'000
Interest on loans from banks and customers	40,614	27,758
Interest on long-term subordinated loans from group undertakings (see note 19)	24,226	21,870
Interest on loans from group undertakings	23,538	36,437
	<b>88,378</b>	<b>86,065</b>

Included in interest on loans from banks and customers is interest on customer deposits and deposits by banks.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**6. PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION**

	Year Ended 31 December 2014 US\$'000	Year Ended 31 December 2013 US\$'000
<b>Profit on ordinary activities before taxation is stated after charging / (crediting):</b>		
Depreciation of tangible fixed assets (see note 14)	190	212
Auditors' remuneration - audit services	290	267
Staff related costs (see note 8)	7,243	8,031
Management fees charged by group undertakings (see note 8)	56,663	54,550
Foreign exchange loss	97	126
Operating lease rentals - land and buildings	344	473
Trading interest payable	234,111	632,309
Trading interest receivable	(248,832)	(531,554)

Trading interest payable and receivable represents interest incurred and generated on the bank's financial instruments classified as held for trading and related financing transactions. This includes coupon interest arising on government bonds, interest on bank loans classified as held for trading, and interest on collateralised agreements and collateralised financing with group undertakings associated with the bank's bond trading business.

The bank has taken the exemption not to disclose fees payable to the auditor and its associates for other non-audit services as such information is required to be disclosed in the consolidated financial statements of Goldman Sachs Group UK Limited ('GSGUK'), the parent company of the smallest group for which consolidated financial statements are prepared.

**7. DIRECTORS' EMOLUMENTS**

	Year Ended 31 December 2014 US\$'000	Year Ended 31 December 2013 US\$'000
Aggregate emoluments	662	514
Company pension contributions to money purchase schemes	2	2
	<b>664</b>	<b>516</b>

	US\$'000	US\$'000
<b>Highest paid director:</b>		
Aggregate emoluments and benefits	238	266
Company pension contributions to money purchase schemes	1	1

In accordance with the Companies Act 2006, directors' emoluments above represent the proportion of total emoluments paid or payable in respect of qualifying services only. This total only includes the value of cash and benefits in kind, and does not include the value of equity awards in accordance with the provisions of Schedule 5 of SI 2008 / 410. Directors also receive emoluments for non-qualifying services which are not required to be disclosed.

Six directors are members of a defined contribution pension plan and four directors are members of a defined benefit pension plan. Seven directors, including the highest paid director, have been granted shares in respect of long-term incentive schemes during the year. Three directors, including the highest paid director, have exercised options during the year.

**GOLDMAN SACHS INTERNATIONAL BANK**  
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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**8. STAFF COSTS**

All persons involved in the bank's operations, other than the Seoul branch and Beijing rep office, are employed by group undertakings. The charges made by these group undertakings, including RSUs, for all the services provided (personnel and other) to the bank are included in the management fees charged by group undertakings (see note 6).

Under Korean and Chinese regulations, the Seoul branch and Beijing rep office are treated as legal entities, hence have the ability to enter into contractual agreements, such as employment, in their own right.

The average number of employees of the Seoul branch and Beijing rep office is analysed below:

	Year Ended 31 December 2014 Number	Year Ended 31 December 2013 Number
<b>Employees:</b>		
Institutional Client Services	8	9
Support Functions	25	22
	<b>33</b>	<b>31</b>

The employment costs incurred by the Seoul branch and Beijing rep office were:

	Year Ended 31 December 2014 US\$'000	Year Ended 31 December 2013 US\$'000
Aggregate gross wages and salaries	6,385	7,197
Employer's National Insurance contributions	335	315
Pension costs, employer contributions to the defined contribution plan	523	519
Total direct costs of employment	<b>7,243</b>	<b>8,031</b>

**9. SHARE-BASED PAYMENTS**

**Stock incentive plan**

Group Inc. sponsors a stock incentive plan, The Goldman Sachs Amended and Restated Stock Incentive Plan (2013) ('the 2013 SIP'), which provides for, amongst others, grants of RSUs and incentive stock options.

The Seoul branch and Beijing rep office recorded share-based compensation in respect of the amortisation of granted equity awards, net of forfeitures of US\$229,345 for the year ended 31 December 2014 (year ended 31 December 2013: US\$631,050). The corresponding credit to equity has been transferred to liabilities as a result of the terms of the intercompany agreements with Group Inc.

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**9. SHARE-BASED PAYMENTS (continued)**

**Restricted stock units**

Group Inc. grants RSUs to the Seoul branch and Beijing rep office's employees under the 2013 SIP, which are valued based on the closing price of the underlying shares on the date of grant after taking into account a liquidity discount for any applicable post-vesting transfer restrictions. RSUs generally vest and underlying shares of common stock deliver as outlined in the applicable RSU agreements. Employee RSU agreements generally provide that vesting is accelerated in certain circumstances, such as on retirement, death, disability and conflicted employment. Delivery of the underlying shares of common stock is conditioned on the grantees satisfying certain vesting and other requirements outlined in the award agreements. The table below presents the activity related to these RSUs:

	31 December 2014		31 December 2013	
	No. of RSUs		No. of RSUs	
	No future service requirement	Future service requirement	No future service requirement	Future service requirement
Outstanding at the beginning of the year	5,065	4,485	4,351	5,156
Granted	373	781	1,364	3,700
Forfeited	-	(642)	-	-
Delivered	(5,050)	-	(4,302)	-
Transferred in / (out)	-	91	-	(719)
Vested	3,195	(3,195)	3,652	(3,652)
<b>Outstanding at the end of the year</b>	<b>3,583</b>	<b>1,520</b>	<b>5,065</b>	<b>4,485</b>

The weighted average grant-date fair value of RSUs granted during the year ended 31 December 2014 was US\$150.06 (year ended 31 December 2013: US\$127.94). The fair value of the RSUs granted during the year ended 31 December 2014 and the year ended 31 December 2013 includes a liquidity discount of 14.7% and 11.9%, respectively, to reflect post-vesting transfer restrictions of up to 4 years.

**10. TAX ON PROFIT ON ORDINARY ACTIVITIES**

**a. Analysis of tax charge for the year:**

	Year Ended 31 December 2014 US\$'000	Year Ended 31 December 2013 US\$'000
<b>Current tax:</b>		
U.K. corporation tax	2,472	16,640
Adjustments in respect of prior periods	(1,968)	342
<b>Total current tax (see note 10b)</b>	<b>504</b>	<b>16,982</b>
<b>Deferred tax:</b>		
Other timing differences (see note 16)	(194)	(46)
<b>Tax on profit on ordinary activities</b>	<b>310</b>	<b>16,936</b>

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**10. TAX ON PROFIT ON ORDINARY ACTIVITIES (continued)**

**b. Factors affecting tax charge for the year:**

The difference between the total current tax shown above and the amount calculated by applying the weighted average rate of U.K. corporation tax applicable to the bank for the year ended 31 December 2014 of 21.5% (year ended 31 December 2013: 23.25%) to the profit on ordinary activities before taxation is as follows:

	Year Ended 31 December 2014 US\$'000	Year Ended 31 December 2013 US\$'000
Profit on ordinary activities before taxation	12,254	68,340
Profit on ordinary activities multiplied by standard rate in the U.K. 21.5% (year ended 31 December 2013: 23.25%)	2,635	15,889
Other timing differences	(118)	67
Expenses not deductible for tax purposes	94	246
Exchange differences	6	438
Utilisation of carried forward losses	(145)	-
Adjustments in respect of prior periods	(1,968)	342
Total current tax	<b>504</b>	<b>16,982</b>

Other timing differences are primarily in respect of share-based compensation and comprise the net tax effect of the amounts charged to the profit and loss account during the year and awards delivered to employees during the year.

Adjustments in respect of prior periods are primarily in relation to the Seoul Branch.

**11. CUSTOMER ACCOUNTS RECEIVABLE**

	31 December 2014 US\$'000	31 December 2013 US\$'000
Amounts due from customers	1,242,473	1,744,796
Amounts due from group undertakings	2,067,053	3,557,461
	<b>3,309,526</b>	<b>5,302,257</b>

Amounts due from customers includes bank loans held at amortised cost of US\$429 million (31 December 2013: US\$31 million).

The following table details the contractual maturity of customer accounts receivable:

	31 December 2014 US\$'000	31 December 2013 US\$'000
Less than three months	2,880,802	5,271,036
More than three months, but less than one year	-	-
More than one year, but less than five years	132,746	31,221
Greater than five years	295,978	-
	<b>3,309,526</b>	<b>5,302,257</b>

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**12. FINANCIAL INSTRUMENTS OWNED AND FINANCIAL INSTRUMENTS SOLD, BUT NOT YET PURCHASED**

Financial instruments owned and financial instruments sold, but not yet purchased comprise financial instruments and investments within the trading activities of the bank. Financial instruments owned pledged as collateral represents financial instruments owned and pledged to group undertakings that have the right to deliver or repledge.

Financial instruments owned, including financial instruments pledged as collateral, comprises:

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>
<b>Cash instruments:</b>		
Government bonds	8,530,999	11,229,056
Bank loans	187,217	441,671
	<b>8,718,216</b>	<b>11,670,727</b>
<b>Derivative instruments:</b>		
Interest rates	7,914,260	4,214,031
Currencies	506,767	358,931
Equities	53,359	5,526
	<b>8,474,386</b>	<b>4,578,488</b>
	<b>17,192,602</b>	<b>16,249,215</b>
Financial instruments owned	9,957,994	7,014,452
Financial instruments owned pledged as collateral	7,234,608	9,234,763
	<b>17,192,602</b>	<b>16,249,215</b>

Financial instruments sold, but not yet purchased comprises:

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>
<b>Cash instruments:</b>		
Government bonds	4,430,870	11,851,141
Bank loans	6,916	14,287
	<b>4,437,786</b>	<b>11,865,428</b>
<b>Derivative instruments:</b>		
Interest rates	7,848,926	4,090,882
Currencies	634,703	406,437
Equities	53,359	5,526
	<b>8,536,988</b>	<b>4,502,845</b>
	<b>12,974,774</b>	<b>16,368,273</b>

**13. COLLATERALISED AGREEMENTS WITH GROUP UNDERTAKINGS**

Of collateralised agreements, US\$22,563 million (31 December 2013: US\$25,929 million) are resale agreements and US\$146 million (31 December 2013: US\$:nil) are other secured lending arrangements.

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**14. TANGIBLE FIXED ASSETS**

The movements in tangible fixed assets during the year were as follows:

	Leasehold improvements US\$'000	Fixtures, fittings & equipment US\$'000	Total US\$'000
<b>Cost</b>			
At 1 January 2014	1,270	2,267	3,537
Additions	185	62	247
Translation gain	51	109	160
At 31 December 2014	<b>1,506</b>	<b>2,438</b>	<b>3,944</b>
<b>Depreciation</b>			
At 1 January 2014	878	2,018	2,896
Charge for the year (see note 6)	48	142	190
Translation loss	39	92	131
At 31 December 2014	<b>965</b>	<b>2,252</b>	<b>3,217</b>
<b>Net Book Value</b>			
At 31 December 2013	<b>392</b>	<b>249</b>	<b>641</b>
At 31 December 2014	<b>541</b>	<b>186</b>	<b>727</b>

**15. OTHER ASSETS**

	31 December 2014 US\$'000	31 December 2013 US\$'000
Other amounts due from group undertakings	729,903	4,863
Deferred tax (see note 16)	507	329
Other assets	11,594	12,272
	<b>742,004</b>	<b>17,464</b>

**16. DEFERRED TAX**

	31 December 2014 US\$'000	31 December 2013 US\$'000
<b>Deferred tax balance comprises (see note 15):</b>		
Other timing differences	507	329
<b>The movements in the deferred tax balance were as follows:</b>		
At 1 January 2014	329	
Transfer to the profit and loss account for the year (see note 10a)	194	
Translation loss	(16)	
At 31 December 2014	<b>507</b>	

Other timing differences mainly relates to deferred tax in respect of share-based compensation.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**17. CUSTOMER ACCOUNTS PAYABLE**

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>
Amounts due to customers	1,888,565	1,351,269
Customer deposits	9,497,616	6,691,719
Deposits from group undertakings	1,168,272	1,366,106
Amounts due to group undertakings	1,297,152	2,494,471
	<b>13,851,605</b>	<b>11,903,565</b>

Customer deposits constitute term deposits designated at fair value through profit or loss of US\$4,356 million (31 December 2013: US\$2,351 million), term deposits held at amortised cost of \$43 million (31 December 2013: US\$nil) and overnight deposits held at amortised cost of US\$5,098 million (31 December 2013: US\$4,341 million). The bank designates term deposits at fair value through profit or loss in order to eliminate the measurement inconsistency that would arise from measuring their related reinvestment, primarily as collateralised agreements with group undertakings, on a different basis.

**18. OTHER LIABILITIES**

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>
Accruals and deferred income	7,360	11,335
Other amounts due to group undertakings	1,531,299	1,466,323
Other liabilities	6,164	1,576
	<b>1,544,823</b>	<b>1,479,234</b>

Other amounts due to group undertakings includes group relief payable of US\$27 million (31 December 2013: US\$30 million).

Other liabilities includes a provision for impairment in respect of the unfunded portion of bank loans held at amortised cost of US\$2 million (31 December 2013: US\$ 1 million).

**19. LONG-TERM SUBORDINATED LOANS FROM GROUP UNDERTAKINGS**

The amounts outstanding as at 31 December 2014 and 31 December 2013 are comprised of two long-term subordinated loans from group undertakings. The loans are unsecured and carry interest at a margin over the U.S. Federal Reserve's federal funds rate. These loans constitute regulatory capital as approved by the PRA, mature on 16 December 2060, and are repayable no earlier than 5 years and 1 day's notice from drawdown date. The repayment of these loans is also subject to PRA approval.

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**20. SHARE CAPITAL**

At 31 December 2014 and 31 December 2013, share capital comprised:

	<b>31 December 2014</b>		<b>31 December 2013</b>	
	<b>No.</b>	<b>US\$'000</b>	<b>No.</b>	<b>US\$'000</b>
<b><u>Allotted, called up and fully paid</u></b>				
Ordinary shares of £1 each	40,169,994	62,558	40,169,994	62,558
		<b>62,558</b>		<b>62,558</b>

On 27 April 2013, 18,956,884 ordinary shares of £1 each were allotted at £37.33 (US\$63.30) to GSGUK. The total contribution received was £785,952,411 (US\$1,200,000,000) in cash incorporating a share premium of £766,995,527 (US\$1,171,056,440). These shares were issued to support the ongoing activities of the bond trading business.

**21. RECONCILIATION OF MOVEMENTS IN TOTAL SHAREHOLDER'S FUNDS AND MOVEMENTS ON RESERVES**

	<b>Called up share capital</b>	<b>Share premium account</b>	<b>Other reserve account</b>	<b>Profit and loss account</b>	<b>Total shareholder's funds</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>At 1 January 2013</b>	<b>33,614</b>	<b>923,247</b>	<b>(12,722)</b>	<b>402,199</b>	<b>1,346,338</b>
Profit for the financial year	-	-	-	51,404	51,404
Shares issued (see note 20)	28,944	1,171,056	-	-	1,200,000
Translation gain	-	-	3,974	-	3,974
Loss on net investment hedge	-	-	(6,401)	-	(6,401)
Share-based payments (see note 9)	-	-	-	631	631
Management recharge related to share-based payments	-	-	-	(631)	(631)
<b>At 1 January 2014</b>	<b>62,558</b>	<b>2,094,303</b>	<b>(15,149)</b>	<b>453,603</b>	<b>2,595,315</b>
Profit for the financial year	-	-	-	11,944	11,944
Translation loss	-	-	(8,674)	-	(8,674)
Gain on net investment hedge	-	-	4,246	-	4,246
Share-based payments (see note 9)	-	-	-	229	229
Management recharge related to share-based payments	-	-	-	(229)	(229)
<b>At 31 December 2014</b>	<b>62,558</b>	<b>2,094,303</b>	<b>(19,577)</b>	<b>465,547</b>	<b>2,602,831</b>

The other reserve account includes the translation gain / (loss) arising on consolidation of the Seoul branch whose functional currency is Korean won and also includes the (loss) / gain on the net investment hedge in respect of the Seoul branch.

**22. FINANCIAL COMMITMENTS AND CONTINGENCIES**

**Commitments**

- a. As at 31 December 2014, the bank had entered into forward starting resale agreements of US\$1,749 million (31 December 2013: US\$101 million). The bank's funding of these commitments depends on the satisfaction of all contractual conditions to the resale agreement and these commitments can expire unused.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**22. FINANCIAL COMMITMENTS AND CONTINGENCIES (continued)**

- b. The bank originates a number of bank loans and a letter of credit which are held as principal risk. The bank also holds bank loans which are sub-participated to group undertakings and third party institutions. The unfunded portion of these agreements, where cash has not been deposited with the bank to collateralise the undrawn commitment, as at 31 December 2014 was US\$2,931 million (31 December 2013: US\$1,532 million) of which US\$1,256 million (31 December 2013: US\$114 million) related to loans sub-participated.
- c. The Seoul branch and Beijing rep office lease certain buildings on long-term leases. Under these leases, which are subject to renegotiation at various intervals specified in the leases, the Seoul branch and Beijing rep office pay all insurance, maintenance and repairs of these properties. The rentals that the Seoul branch and Beijing rep office is committed to pay in the next year are as follows:

	31 December 2014	31 December 2013
	US\$'000	US\$'000
<b>Maturity of lease:</b>		
Less than one year	167	24
Between one and two years	-	-
Between two and five years	-	-
Over five years	438	360
	<b>605</b>	<b>384</b>

**Contingent liabilities**

- a. In the prior year, the bank had a contingent liability to tax authorities in relation to the guarantee of certain tax obligations of Goldman Sachs (UK) L.L.C. and Goldman Sachs Group Holdings (U.K.) Limited. During the current year, the guarantee expired unused. The present value of the guarantee as at 31 December 2013 was US\$2 million. The guarantee was covered by a back to back guarantee with the ultimate parent company, Group Inc.
- b. The bank, in its capacity as an agency lender, indemnifies most of its securities lending customers against losses incurred in the event that borrowers do not return securities. The maximum exposure to loss under guarantee at year end is US\$2,405 million (31 December 2013: US\$1,897 million). The market value of the collateral held to cover the loss was \$2,649 million (31 December 2013: US\$2,013 million). These guarantees are covered by back to back guarantees with the ultimate parent company, Group Inc. These guarantees were not utilised during the current or prior years.
- c. The bank had a contingent liability to the minority shareholders of an Oslo Børs listed entity in relation to a squeeze-out guarantee, issued by the bank as part of its lending activities, in connection with a compulsory acquisition of shares. The present value of the guarantee as at 31 December 2014 was US\$10 million (31 December 2013: US\$nil). The guarantee expired unused in January 2015.

**23. FINANCIAL RISK MANAGEMENT**

Normal activities expose the bank to market, credit and liquidity risk. These risks, described below, are managed in accordance with established risk management policies and procedures.

The group manages market, credit and liquidity risk on a consistent basis firmwide. Consequently, the bank, as part of the group, adheres to global risk management policies and procedures.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

The bank seeks to monitor and control risk exposure through a risk and control framework encompassing a variety of separate, but complementary financial, credit, operational, compliance and legal reporting systems, internal controls, management review processes and other mechanisms. In addition, a number of global, regional and entity committees are responsible for monitoring risk exposures and for general oversight of the bank's risk management process. These committees meet regularly and consist of senior members of both the revenue-producing units and departments that are independent of the revenue-producing units. In addition to these committees, functions that are independent of the revenue-producing units, such as compliance, finance (including risk management), legal, internal audit and operations, perform global risk management functions, which include monitoring, analysing and evaluating risk.

**a. Market risk**

**Overview**

Market risk is the risk of loss in the value of inventory, as well as certain other financial assets and financial liabilities, due to changes in market conditions. The bank employs a variety of risk measures, each described in the respective sections below, to monitor market risk. The bank holds inventory primarily for market-making for clients. Inventory therefore changes based on client demands. The bank's inventory is accounted for at fair value and therefore fluctuates on a daily basis, with the related gains and losses included in trading profit. Categories of market risk include the following:

- Interest rate risk: results from exposures to changes in the level, slope and curvature of yield curves, the volatilities of interest rates and credit spreads;
- Currency rate risk: results from exposures to changes in spot prices, forward prices and volatilities of currency rates; and
- Equity price risk: results from exposures to changes in prices and volatilities of individual equities, baskets of equities and equity indices.

**Market risk management process**

The bank manages market risk by diversifying exposures, controlling position sizes and establishing economic hedges in related securities or derivatives. This includes:

- Accurate and timely exposure information incorporating multiple risk metrics;
- A dynamic limit setting framework; and
- Constant communication amongst revenue-producing units, risk managers and senior management.

The bank's framework for managing market risk is consistent with, and part of, the group's framework, and results are analysed by business and in aggregate, at both the group and bank level.

Market Risk Management, which is independent of the revenue-producing units and reports to the group's chief risk officer, has primary responsibility for assessing, monitoring and managing market risk. Risks are monitored and controlled through strong oversight and independent control and support functions across the global businesses.

Managers in revenue-producing units are accountable for managing risk within prescribed limits, both at the group and bank level. These managers have in-depth knowledge of their positions, markets and the instruments available to hedge their exposures.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**a. Market risk (continued)**

Managers in revenue-producing units and Market Risk Management discuss market information, positions and estimated risk and loss scenarios on an ongoing basis.

**VaR**

VaR is the potential loss in value of financial instruments due to adverse market movements over a defined time horizon with a specified confidence level. A one-day time horizon with a 95% confidence level is typically employed.

The table below sets forth year-end VaR, average daily VaR, as well as high and low VaR for the year.

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'millions</b>	<b>US\$'millions</b>
Total VaR at	1.6	3.4
Average daily VaR for the year ended	2.0	4.0
Highest daily VaR for the year ended	8.1	7.4
Lowest daily VaR for the year ended	0.8	1.6

**b. Credit risk**

**Overview**

Credit risk represents the potential for loss due to the default or deterioration in credit quality of a counterparty (e.g. an OTC derivatives counterparty or a borrower) or an issuer of securities or other instruments the bank holds. Exposure to credit risk comes mostly from client transactions in OTC derivatives and lending activities. Credit risk also comes from cash placed with banks, resale and repurchase agreements, and receivables from brokers / dealers, clearing organisations, customers and counterparties.

Credit Risk Management, which is independent of the revenue-producing units and reports to the group's chief risk officer, has primary responsibility for assessing, monitoring and managing credit risk. The bank's framework for managing credit risk is consistent with the framework of the group. The group's Credit Policy Committee and Firmwide Risk Committee establish and review credit policies and parameters for the group as a whole. In addition, the bank holds other positions that give rise to credit risk, (e.g. government bonds). These credit risks are captured as a component of market risk measures, which are monitored and managed by Market Risk Management. The bank also enters into derivatives to manage market risk exposures. Such derivatives also give risk to credit risk which is monitored by Credit Risk Management.

Policies authorised by the group's Firmwide Risk Committee and Credit Policy Committee prescribe the level of formal approval required for the group to assume credit exposure to a counterparty across all product areas, taking into account any applicable netting provisions, collateral or other credit risk mitigants. These policies are complemented by specific policies for the bank, which are approved by the bank's governance bodies, including the bank's Risk Committee.

**Credit risk management process**

Effective management of credit risk requires accurate and timely information, a high level of communication and knowledge of customers, countries, industries and products. The process for managing credit risk includes:

- Approving transactions and setting and communicating credit exposure limits;
- Monitoring compliance with established credit exposure limits;

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**b. Credit risk (continued)**

- Assessing the likelihood that a counterparty will default on its payment obligations;
- Measuring the bank's current and potential credit exposure and losses resulting from counterparty default;
- Reporting of credit exposures to senior management, the bank's board and regulators;
- Use of credit risk mitigants, including collateral and hedging; and
- Communication and collaboration with other independent control and support functions such as operations, legal and compliance.

As part of the risk assessment process, Credit Risk Management performs credit reviews which include initial and ongoing analyses of the bank's counterparties. For substantially all of the bank's credit exposures, the core of the process is an annual counterparty credit review. A credit review is an independent analysis of the capacity and willingness of a counterparty to meet its financial obligations, resulting in an internal credit rating. The determination of internal credit ratings also incorporates assumptions with respect to the nature of and outlook for the counterparty's industry and the economic environment. Senior personnel within Credit Risk Management, with expertise in specific industries, inspect and approve credit reviews and internal credit ratings.

The global credit risk management systems capture credit exposure to individual counterparties and, on an aggregate basis, to counterparties and their subsidiaries (economic groups). These systems also provide management with comprehensive information on aggregate credit risk by product, internal credit rating, industry, country and region.

**Credit exposures**

The bank's credit exposures are described further below.

**Cash at bank and in hand.** Cash at bank and in hand includes both interest-bearing and non-interest bearing deposits. To mitigate the risk of credit loss, the bank places substantially all of its deposits with highly-rated banks and central banks.

**Customer accounts receivable.** The bank is exposed to credit risk from its customer accounts receivable through its amounts due from customers and amounts due from group undertakings. These primarily comprise receivables related to sales of securities which have traded, but not yet settled. These receivables generally have minimal credit risk due to the low probability of clearing organisation default and the short-term nature of receivables related to securities settlements. Customer accounts receivable also includes bank loans held at amortised cost. The bank manages its lending activities using the processes described above, including participation agreements with affiliates.

**Financial instruments owned.** Financial instruments owned includes cash instruments and derivatives. In the table below cash instruments are included in the gross exposure; however to the extent that they have been captured by market risk they are removed to arrive at net credit exposure. Derivatives are reported at fair value on a gross by counterparty basis in the bank's financial statements unless it has current legal right of set off and also intends to settle on a net basis. OTC derivatives are risk managed using the risk processes, measures and limits described above.

**Collateralised agreements with group undertakings.** The bank bears credit risk related to resale agreements only to the extent that cash advanced to the counterparty exceeds the value of the collateral received. The bank's credit exposure on these transactions is therefore significantly lower than the amounts recorded on the balance sheet, which represent fair values or contractual value before consideration of collateral received. The bank also has credit exposure on repurchase agreements, which are liabilities on its balance sheet, to the extent that the value of collateral pledged to the counterparty for these transactions exceeds the amount of cash or collateral received.

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**23. FINANCIAL RISK MANAGEMENT (continued)**

**b. Credit risk (continued)**

The table below presents the bank's gross credit exposure to financial assets and net credit exposure after taking account of assets captured by market risk in the bank's risk management process, enforceable master netting agreements, the value of collateral received in respect of financial assets and the value of cash collateral posted in respect of derivative liabilities.

Amounts in respect of master netting agreements include the offsetting of derivative assets with liabilities and resale agreements with repurchase agreements. Derivatives are reported on a net-by-counterparty basis (i.e. the net payable or receivable for derivative assets and liabilities for a given counterparty) when a legal right of set off exists under an enforceable netting agreement. Resale and repurchase agreements with the same term and currency are presented on a net-by-counterparty basis when such transactions meet certain settlement criteria and are subject to netting agreements. Cash and security collateral have been offset to the extent there are credit exposures on the balance sheet.

**Credit exposure by financial asset class**

	<b>31 December 2014</b>					
	<b>Gross exposure</b>	<b>Assets captured by market risk</b>	<b>Master netting agreements</b>	<b>Cash collateral</b>	<b>Security collateral received</b>	<b>Net credit exposure</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Financial asset class:</b>						
Cash at bank and in hand	115,919	-	-	-	-	115,919
Customer accounts receivable	3,309,526	-	-	(525,628)	(295,613)	2,488,285
Financial instruments owned	9,957,994	(1,296,391)	(7,970,012)	(239,923)	(53,331)	398,337
Financial instruments owned pledged as collateral	7,234,608	(7,234,608)	-	-	-	-
Collateralised agreements with group undertakings	22,709,036	-	-	-	(22,709,036)	-
Other assets	742,004	-	-	-	-	742,004
	<b>44,069,087</b>	<b>(8,530,999)</b>	<b>(7,970,012)</b>	<b>(765,551)</b>	<b>(23,057,980)</b>	<b>3,744,545</b>

	<b>31 December 2013</b>					
	<b>Gross exposure</b>	<b>Assets captured by market risk</b>	<b>Master netting agreements</b>	<b>Cash collateral</b>	<b>Security collateral received</b>	<b>Net credit exposure</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Financial asset class:</b>						
Cash at bank and in hand	128,808	-	-	-	-	128,808
Customer accounts receivable	5,302,257	-	-	(134,143)	-	5,168,114
Financial instruments owned	7,014,452	(1,994,293)	(4,180,426)	(52,352)	-	787,381
Financial instruments owned pledged as collateral	9,234,763	(9,234,763)	-	-	-	-
Collateralised agreements with group undertakings	25,929,110	-	-	-	(25,929,110)	-
Other assets	17,464	-	-	-	-	17,464
	<b>47,626,854</b>	<b>(11,229,056)</b>	<b>(4,180,426)</b>	<b>(186,495)</b>	<b>(25,929,110)</b>	<b>6,101,767</b>

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**23. FINANCIAL RISK MANAGEMENT (continued)**

**b. Credit risk (continued)**

The table below presents the bank's gross and net credit exposure to financial assets based on internally determined public rating agency equivalents based on internal credit ratings.

**Credit exposure by credit rating equivalent**

	<b>31 December 2014</b>					
	<b>Gross exposure</b>	<b>Assets captured by market risk</b>	<b>Master netting agreements</b>	<b>Cash collateral</b>	<b>Security collateral received</b>	<b>Net credit exposure</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Credit rating equivalent:</b>						
AAA/Aaa	4,605	-	-	-	-	4,605
AA/Aa	474,258	-	(66,277)	(3,018)	(38,581)	366,382
A/A	34,135,155	-	(7,877,341)	(756,730)	(22,709,036)	2,792,048
BBB/Baa2	277,451	-	(24,744)	(5,400)	(14,750)	232,557
BB/Ba2 or lower	429,165	-	(1,650)	(403)	(226,650)	200,462
Unrated	8,748,453	(8,530,999)	-	-	(68,963)	148,491
	<b>44,069,087</b>	<b>(8,530,999)</b>	<b>(7,970,012)</b>	<b>(765,551)</b>	<b>(23,057,980)</b>	<b>3,744,545</b>

	<b>31 December 2013</b>					
	<b>Gross exposure</b>	<b>Assets captured by market risk</b>	<b>Master netting agreements</b>	<b>Cash collateral</b>	<b>Security collateral received</b>	<b>Net credit exposure</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Credit rating equivalent:</b>						
AAA/Aaa	3,095	-	-	-	-	3,095
AA/Aa	717,439	-	-	(2,910)	-	714,529
A/A	34,793,696	-	(4,179,938)	(183,585)	(25,929,110)	4,501,063
BBB/Baa2	117,985	-	(488)	-	-	117,497
BB/Ba2 or lower	563,809	-	-	-	-	563,809
Unrated	11,430,830	(11,229,056)	-	-	-	201,774
	<b>47,626,854</b>	<b>(11,229,056)</b>	<b>(4,180,426)</b>	<b>(186,495)</b>	<b>(25,929,110)</b>	<b>6,101,767</b>

As at the current and prior year ends, financial assets past due or impaired were insignificant.

**Collateralised transactions**

The bank receives financial instruments as collateral, primarily in connection with resale agreements and derivative transactions. Such financial instruments may include obligations of sovereigns, agencies and corporations as well as equities and convertibles. In many cases, the bank is permitted to deliver or repledge these financial instruments in connection with entering into repurchase agreements, collateralising derivatives and meeting firm or customer settlement requirements.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**b. Credit risk (continued)**

As at 31 December 2014, the fair value of financial instruments received as collateral and which the bank is permitted to deliver or repledge was \$21,632 million (31 December 2013: \$25,159 million), of which the bank delivered or repledged US\$5,388 million (31 December 2013: US\$11,003 million). Following a review of internal collateral allocations, the fair value of financial instruments received as collateral which the bank delivered or repledged as at 31 December 2013 has been revised from \$23,398 million to US\$11,003 million. The revision does not impact the profit and loss account, the statement of total recognised gains and losses or the balance sheet.

The bank also pledges financial assets that they own to group undertakings who have the right to deliver or repledge. These amounts are included within 'Financial instruments owned pledged as collateral' in the financial statements and were US\$7,235 million as at 31 December 2014 (31 December 2013: US\$9,235 million).

The bank has posted cash collateral in respect of financial instruments of US\$526 million (31 December 2013: US\$134 million).

**c. Liquidity risk**

**Overview**

Liquidity risk is the risk that the bank does not have sufficient cash or collateral to make payments to its counterparties and customers as they fall due. Liquidity is of critical importance to financial institutions. Most of the failures of financial institutions have occurred in part due to insufficient liquidity. Accordingly, the bank has in place a comprehensive and conservative set of liquidity and funding policies to address both bank-specific and broader industry or market liquidity events. The principal objective is to be able to fund the bank and to enable the core businesses to continue to serve clients and generate revenues, even under adverse circumstances.

**Liquidity risk management principles**

The bank manages liquidity risk according to the following principles:

- Liquidity – maintain substantial liquidity to meet a broad range of potential cash outflows and collateral needs in a stressed environment;
- Asset-liability management – assess anticipated holding periods for the bank's assets and their expected liquidity in a stressed environment, manage maturities and diversity of funding across markets, products and counterparties, and seek to maintain liabilities of appropriate tenor relative to the asset base; and
- Contingency funding plan ('CFP') – the bank maintains a CFP, which is an addendum to the group's CFP. The contingency funding plan provides a framework for analysing and responding to a liquidity crisis situation or periods of market stress. This framework sets forth the plan of action to fund normal business activity in emergency and stress situations.

The following table details the bank's cash flows of its financial liabilities by contractual maturity including interest that will accrue, except for financial instruments sold, but not yet purchased. Financial instruments sold, but not yet purchased are classified as trading / on demand. Financial liabilities, with the exception of those that are held for trading or designated at fair value through profit and loss, are disclosed at their undiscounted cash flows. The fair values of financial liabilities held for trading and financial liabilities designated at fair value through profit and loss have been disclosed as this is consistent with the values used in the liquidity risk management of these instruments. Liquidity risk on derivatives is mitigated through master netting agreements and cash collateral arrangements.

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**23. FINANCIAL RISK MANAGEMENT (continued)**

**c. Liquidity risk (continued)**

31 December 2014							
	Trading / on demand	Less than one month	More than one month, but less than three months	More than three months, but less than one year	More than one year, but less than five years	Greater than five years	Total
	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000
<b>Financial liabilities:</b>							
Customer accounts payable	5,097,945	5,056,780	1,192,072	2,454,402	10,638	42,322	13,854,159
Deposits by banks	-	720,884	1,600,718	971,078	-	-	3,292,680
Financial instruments sold, but not yet purchased	12,974,774	-	-	-	-	-	12,974,774
Collateralised financing with group undertakings	-	34,830	-	8,942,089	-	-	8,976,919
Other liabilities	-	715,784	-	754,425	-	74,614	1,544,823
Long-term subordinated loans from group undertakings	-	-	5,907	17,722	873,314	-	896,943
<b>Total – on-balance sheet</b>	<b>18,072,719</b>	<b>6,528,278</b>	<b>2,798,697</b>	<b>13,139,716</b>	<b>883,952</b>	<b>116,936</b>	<b>41,540,298</b>
Total – commitments	-	4,680,010	-	605	-	-	4,680,615
<b>Total</b>	<b>18,072,719</b>	<b>11,208,288</b>	<b>2,798,697</b>	<b>13,140,321</b>	<b>883,952</b>	<b>116,936</b>	<b>46,220,913</b>

31 December 2013							
	Trading / on demand	Less than one month	More than one month, but less than three months	More than three months, but less than one year	More than one year, but less than five years	Greater than five years	Total
	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000
<b>Financial liabilities:</b>							
Customer accounts payable	8,497,372	110,393	2,507,167	792,458	-	-	11,907,390
Deposits by banks	-	-	758,795	1,773,713	-	-	2,532,508
Financial instruments sold, but not yet purchased	16,368,273	-	-	-	-	-	16,368,273
Collateralised financing with group undertakings	-	-	-	11,926,181	-	-	11,926,181
Other liabilities	1,360,670	23	24,958	-	6,432	87,151	1,479,234
Long-term subordinated loans from group undertakings	-	-	5,866	17,598	896,388	-	919,852
<b>Total – on-balance sheet</b>	<b>26,226,315</b>	<b>110,416</b>	<b>3,296,786</b>	<b>14,509,950</b>	<b>902,820</b>	<b>87,151</b>	<b>45,133,438</b>
Total – commitments	-	1,633,669	-	-	-	-	1,633,669
<b>Total</b>	<b>26,226,315</b>	<b>1,744,085</b>	<b>3,296,786</b>	<b>14,509,950</b>	<b>902,820</b>	<b>87,151</b>	<b>46,767,107</b>

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**d. Transferred financial assets**

The bank enters into collateralised financing with group undertakings where certain financial assets are transferred as collateral. The financial asset collateral continues to be recognised in full and the related financial liability reflecting the bank's obligation to repurchase the transferred financial assets, at a future date, is recognised in collateralised financing with group undertakings. The bank remains exposed to market and credit risk on these pledged financial assets. The counterparties' recourse is not limited to the transferred financial assets.

The fair value of the financial assets subject to repurchase was US\$7,235 million (31 December 2013: US\$9,235 million) and their related financial liabilities funded at 1% - 1.15% below the fair value of the financial asset collateral pledged.

**e. Financial instruments by category**

The table below presents the carrying value of the bank's financial assets and financial liabilities by category.

	<b>31 December 2014</b>				
	<b>Held for trading</b>	<b>Designated at fair value</b>	<b>Loans and receivables</b>	<b>Amortised cost</b>	<b>Total carrying value</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Financial assets:</b>					
Cash at bank and in hand	-	-	115,919	-	115,919
Customer accounts receivable	-	-	3,309,526	-	3,309,526
Financial instruments owned	9,957,994	-	-	-	9,957,994
Financial instruments owned pledged as collateral	7,234,608	-	-	-	7,234,608
Collateralised agreements with group undertakings	-	22,709,036	-	-	22,709,036
Other assets	-	-	742,004	-	742,004
<b>Total financial assets</b>	<b>17,192,602</b>	<b>22,709,036</b>	<b>4,167,449</b>	<b>-</b>	<b>44,069,087</b>
<b>Financial liabilities:</b>					
Customer accounts payable	-	4,356,392	-	9,495,213	13,851,605
Deposits by banks	-	3,292,680	-	-	3,292,680
Financial instruments sold, but not yet purchased	12,974,774	-	-	-	12,974,774
Collateralised financing with group undertakings	-	8,976,919	-	-	8,976,919
Other liabilities	-	-	-	1,544,823	1,544,823
Long-term subordinated loans from group undertakings	-	-	-	826,182	826,182
<b>Total financial liabilities</b>	<b>12,974,774</b>	<b>16,625,991</b>	<b>-</b>	<b>11,866,218</b>	<b>41,466,983</b>

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**e. Financial instruments by category (continued)**

	31 December 2013				
	Held for trading	Designated at fair value	Loans and receivables	Amortised cost	Total carrying value
	US\$'000	US\$'000	US\$'000	US\$'000	US\$'000
<b>Financial assets:</b>					
Cash at bank and in hand	-	-	128,808	-	128,808
Customer accounts receivable	-	-	5,302,257	-	5,302,257
Financial instruments owned	7,014,452	-	-	-	7,014,452
Financial instruments owned pledged as collateral	9,234,763	-	-	-	9,234,763
Collateralised agreements with group undertakings	-	25,929,110	-	-	25,929,110
Other assets	-	-	17,464	-	17,464
<b>Total financial assets</b>	<b>16,249,215</b>	<b>25,929,110</b>	<b>5,448,529</b>	<b>-</b>	<b>47,626,854</b>
<b>Financial liabilities:</b>					
Customer accounts payable	-	2,350,694	-	9,552,871	11,903,565
Deposits by banks	-	2,528,745	-	-	2,528,745
Financial instruments sold, but not purchased	16,368,273	-	-	-	16,368,273
Collateralised financing with group undertakings	-	11,926,181	-	-	11,926,181
Other liabilities	-	-	-	1,479,234	1,479,234
Long-term subordinated loans from group undertakings	-	-	-	826,182	826,182
<b>Total financial liabilities</b>	<b>16,368,273</b>	<b>16,805,620</b>	<b>-</b>	<b>11,858,287</b>	<b>45,032,180</b>

**f. Fair value hierarchy**

The fair values for substantially all of the bank's financial assets and financial liabilities are based on observable prices and inputs and are classified in levels 1 and 2 of the fair value hierarchy. Certain level 2 and level 3 financial assets and financial liabilities may require appropriate valuation adjustments that a market participant would require to arrive at fair value for factors such as counterparty and the bank's credit quality, funding risk, transfer restrictions, illiquidity and bid / offer spreads. Valuation adjustments are generally based on market evidence.

The following table presents the level within the fair value hierarchy of financial instruments owned at fair value and financial instruments sold, but not yet purchased, at fair value and other financial assets and financial liabilities designated at fair value through profit or loss.

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**23. FINANCIAL RISK MANAGEMENT (continued)**

**f. Fair value hierarchy (continued)**

<b>31 December 2014</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Financial assets at fair value:</b>				
Financial instruments owned, including financial instruments owned pledged as collateral	8,462,542	8,502,228	227,832	17,192,602
Collateralised agreements with group undertakings	-	22,709,036	-	22,709,036
<b>Total financial assets at fair value</b>	<b>8,462,542</b>	<b>31,211,264</b>	<b>227,832</b>	<b>39,901,638</b>

**Financial liabilities at fair value:**

Customer accounts payable	-	4,356,392	-	4,356,392
Deposits by banks	-	3,292,680	-	3,292,680
Financial instruments sold, but not yet purchased	4,391,873	8,509,423	73,478	12,974,774
Collateralised financing with group undertakings	-	8,976,919	-	8,976,919
<b>Total financial liabilities at fair value</b>	<b>4,391,873</b>	<b>25,135,414</b>	<b>73,478</b>	<b>29,600,765</b>

<b>31 December 2013</b>				
	<b>Level 1</b>	<b>Level 2</b>	<b>Level 3</b>	<b>Total</b>
	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>	<b>US\$'000</b>
<b>Financial assets at fair value:</b>				
Financial instruments owned, including financial instruments owned pledged as collateral	11,086,295	4,819,969	342,951	16,249,215
Collateralised agreements with group undertakings	-	25,929,110	-	25,929,110
<b>Total financial assets at fair value</b>	<b>11,086,295</b>	<b>30,749,079</b>	<b>342,951</b>	<b>42,178,325</b>

**Financial liabilities at fair value:**

Customer accounts payable	-	2,350,694	-	2,350,694
Deposits by banks	-	2,528,745	-	2,528,745
Financial instruments sold, but not yet purchased	11,744,000	4,604,291	19,982	16,368,273
Collateralised financing with group undertakings	-	11,926,181	-	11,926,181
<b>Total financial liabilities at fair value</b>	<b>11,744,000</b>	<b>21,409,911</b>	<b>19,982</b>	<b>33,173,893</b>

During the year ended 31 December 2014, there were no significant transfers between level 1 and 2 financial assets and financial liabilities. The following table presents the changes in fair value for all the financial assets and financial liabilities categorised as level 3.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**f. Fair value hierarchy (continued)**

	Financial instruments owned	Financial instruments sold, but not yet purchased
	US\$'000	US\$'000
<b>Reconciliation of level 3 financial instruments at fair value:</b>		
At 1 January 2014	342,951	(19,982)
Profit / (loss) for the financial year	10,025	(20,787)
Purchases	128,832	2,699
Sales	(123,107)	(43,122)
Settlements	(130,809)	7,714
Transfers out of level 3	(60)	-
<b>At 31 December 2014</b>	<b>227,832</b>	<b>(73,478)</b>

	Financial instruments owned	Financial instruments sold, but not yet purchased
	US\$'000	US\$'000
<b>Reconciliation of level 3 financial instruments at fair value:</b>		
At 1 January 2013	43,411	(33,726)
Profit for the financial year	5,260	2,794
Purchases	321,075	(344)
Sales	(5)	(12,917)
Settlements	(26,790)	24,211
<b>At 31 December 2013</b>	<b>342,951</b>	<b>(19,982)</b>

The fair value of financial instruments may be determined in whole or in part using a valuation technique based on assumptions that are not supported by prices from observable current market transactions in the same financial instrument or based on available observable market data and changing these assumptions will change the resultant estimate of fair value. The potential impact as at 31 December 2014 of using reasonable possible alternative assumptions for the valuations including significant unobservable inputs has been quantified as approximately US\$12 million (31 December 2013: US\$5 million) for favourable changes and US\$14 million (31 December 2013: US\$5 million) for unfavourable changes.

The fair value of customer deposits and deposits by banks designated at fair value through profit or loss as at 31 December 2014 was US\$7,649 million (31 December 2013: US\$4,879 million). The impact of changes in the fair value of these deposits driven by changes in the bank's credit spreads during the year ended 31 December 2014 and cumulatively was immaterial.

**g. Fair value of financial instruments not measured at fair value**

For financial assets and financial liabilities not measured at fair value, the carrying amounts in the balance sheet are a reasonable approximation of fair value given the short-term nature of these financial instruments, with the exception of the below:

	31 December 2014		31 December 2013	
	Carrying value	Approximate fair value	Carrying value	Approximate fair value
	US\$'000	US\$'000	US\$'000	US\$'000
Long-term subordinated loans from group undertakings	826,182	854,649	826,182	861,869

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**g. Fair value of financial instruments not measured at fair value (continued)**

Long-term subordinated loans from group undertakings are repayable no earlier than 5 years and 1 day's notice from drawdown date. The fair value of these loans has been determined on the assumption that these loans are repaid on their earliest potential repayment date, although repayment is subject to PRA approval.

The bank also has commitments in respect of the unfunded portion of bank loans held at amortised cost. The approximate value of the financial liability the bank would record in respect of these commitments, were they held at fair value, would be US\$32 million as at 31 December 2014 (31 December 2013: US\$28 million).

**h. Hedge accounting**

The bank designates certain interest rate swaps as fair value hedges. These interest rate swaps hedge changes in fair value attributable to the relevant benchmark interest rate (e.g., London Interbank Offered Rate ('LIBOR')), effectively converting fixed-rate obligations into floating-rate obligations.

The bank applies a statistical method that utilises regression analysis when assessing the effectiveness of its fair value hedging relationships in achieving offsetting changes in the fair values of the hedging instrument and the risk being hedged (i.e., interest rate risk). An interest rate swap is considered highly effective in offsetting changes in fair value attributable to changes in the hedged risk when the regression analysis results in a coefficient of determination of 80% or greater and a slope between 80% and 125%.

For qualifying fair value hedges, gains or losses on derivatives and the change in fair value of the hedged item attributable to the hedged risk are included in trading profit. When a derivative is no longer designated as a hedge, any remaining difference between the carrying value and par value of the hedged item is amortised over the remaining life of the hedged item using the effective interest method.

The table below presents the gains / (losses) from interest rate derivatives accounted for as hedges, the related hedged customer deposits and the hedge ineffectiveness on these derivatives.

	<b>31 December 2014</b>	<b>31 December 2013</b>
	<b>US\$'000</b>	<b>US\$'000</b>
Interest rate hedges	142	-
Hedged customer deposits	(136)	-
<b>Ineffectiveness</b>	<b>6</b>	<b>-</b>

**i. Capital management**

The bank is authorised by the PRA and regulated by the FCA and PRA and as such is subject to examination by the PRA and to minimum capital adequacy standards. In implementing the Capital Requirements Directive ('CRD') the PRA requires each bank and banking group to maintain an individually prescribed ratio of capital to risk weighted assets. The bank monitored and demonstrated compliance with the relevant regulatory capital requirements of the PRA at all times during the year.

The level and composition of the bank's capital is principally determined by its regulatory capital requirements, but may also be influenced by the business environment, conditions in the financial markets and assessments of potential future losses due to extreme and adverse changes in the bank's businesses and market environment.

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**NOTES TO THE FINANCIAL STATEMENTS - 31 DECEMBER 2014**

**23. FINANCIAL RISK MANAGEMENT (continued)**

**i. Capital management (continued)**

For regulatory purposes, the bank's capital is divided into two tiers:

As at 31 December 2014:

- Tier 1 capital - US\$2,603 million (31 December 2013: US\$2,595 million) - comprises called up share capital, share premium account, other reserve account, and the profit and loss account.
- Tier 2 capital - US\$826 million (31 December 2013: US\$826 million) - solely comprises long-term subordinated loans from group undertakings.

Various regulatory limits and deductions are applied.

**24. POST BALANCE SHEET EVENTS**

On 30 January 2015, to support growth in the bank's lending activities, the bank established a branch in Germany.

**25. OTHER ITEMS**

**Basel III Pillar 3 disclosures**

The bank is included in the consolidated Pillar 3 disclosures of Goldman Sachs Group UK Limited ('GSGUK'), which are required by the EU Capital Requirements Regulation. GSGUK's 2014 Pillar 3 disclosures will be made available, in conjunction with the publication of its financial statements, at [www.goldmansachs.com/disclosures/](http://www.goldmansachs.com/disclosures/).

**Country-by-country reporting**

The bank is included in the consolidated country-by-country reporting disclosures of GSGUK, which are required by the Capital Requirements (Country-by-Country Reporting) Regulations 2013. GSGUK's 2014 country-by-country disclosures will be made available by 31 December 2015 at [www.goldmansachs.com/disclosures/](http://www.goldmansachs.com/disclosures/).

**26. ULTIMATE AND IMMEDIATE PARENT UNDERTAKINGS**

The immediate parent undertaking and the parent company of the smallest group for which consolidated financial statements are prepared is Goldman Sachs Group UK Limited, a company incorporated and registered in England and Wales. Copies of its consolidated financial statements are available on request from The Company Secretary, Goldman Sachs Group UK Limited, Peterborough Court, 133 Fleet Street, London, EC4A 2BB, United Kingdom:

The ultimate controlling undertaking and the parent company of the largest group for which consolidated financial statements are prepared is The Goldman Sachs Group, Inc., a company incorporated in the United States of America. Copies of its consolidated financial statements, as well as certain regulatory filings, for example Quarterly Report on Form 10-Q and Annual Report on Form 10-K, that provide additional information on the group and its business activities, can be obtained from Investor Relations, 200 West Street, New York, NY 10282, United States of America, the group's principal place of business or at [www.goldmansachs.com/shareholders/](http://www.goldmansachs.com/shareholders/).