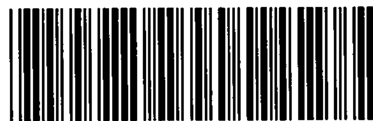
FINANCIAL STATEMENTS

31 DECEMBER 2017

COMPANY NUMBER: 1698498



MUFG Securities EMEA plc
A member of MUFG, a global financial group

MUFG

2018 Mitsubishi UFJ Financial Group

Strategic Report

The Strategic report is prepared in accordance with The Companies Act 2006 (Strategic Report and Directors' Report) Regulations 2013.

Principal activities

MUFG Securities EMEA plc ("MUS(EMEA)" or "the Company") is the international capital markets subsidiary of Mitsubishi UFJ Securities Holdings Co., Ltd. ("MUSHD"). MUSHD's parent, and MUS(EMEA)'s ultimate holding company, is Mitsubishi UFJ Financial Group, Inc. ("MUFG").

MUS(EMEA) actively trades in fixed income, equity and structured finance products, providing client solutions across primary and secondary markets. The client group includes financial institutions, corporations and central banks. The Company primarily supports this client group from its base in London and additionally operates a branch in the Dubai International Financial Centre. The principal activities of the Company remain largely consistent with those disclosed in previous years.

Results

The results for the year are set out on page 19 and the profit for the year, after tax, amounted to £79.8 million (2016: £59.9 million). The financial statements of the Company are prepared in accordance with International Financial Reporting Standards ("IFRS") as adopted by the European Union.

Business review and future development

The Company has achieved a record year for both revenue and profit, with strong performances in most product areas, coupled with continued focus on cost control. The revenue performance is of particular significance given the challenges and general market uncertainty faced throughout the year. Of those challenges, the UK Referendum on EU Membership ("Brexit") continues to be an important consideration, as well as the persistent low interest rate environment and general market uncertainty. Ongoing management of the cost base has been key to supporting growth in profitability with additional spend focussed on supporting key initiatives as well as appropriate levels of investment to ensure continued compliance with evolving regulatory requirements.

Collaboration with colleagues across the MUFG network has increased our ability to support clients to access global capital markets. Geographically, our Middle East operations have been further expanded with the launch of a markets sales franchise during the year.

The Rates desk continues to be the main revenue driver, with both primary and secondary desks delivering another strong performance in 2017. Fixed income cash trading volumes have increased, client hedging including FX facilitation has been strong and spread revenues achieved within secured financing trades remains at record levels. The Structured business has delivered impressive results supporting the core Japanese investor base with parallel initiatives supporting product diversification. Overall, there has been a strong and successful focus towards client activity led by our sales force.

Improved revenue results have been achieved whilst maintaining Value at Risk ("VaR") metrics within internal limits set by the Board of Directors ("the Board"). These metrics reflect management's focus on client-led revenues and targeted risk taking, with capital deployment and associated risk management applied where appropriate.

In line with new regulations, specifically Basel III Leverage Ratio requirements, management has adopted a framework of leverage based constraints reflective of industry norms and the Company's high quality and predominantly liquid balance sheet. In line with this approach a number of actions including a range of balance sheet efficiency measures as well as strategy rationalisation were concluded during the year. The impact of this programme is evident in our balance sheet, where exposures have materially reduced through 2017. The related profitability impact has been mitigated through an intelligent and selective approach to deployment of available capacity as well as ensuring efficiency through new initiatives such as derivative compression. The regulation is currently evolving, with recent industry consultations on the topic potentially impacting final requirements as well as timing.

The Company manages and monitors its capital base to ensure that sufficient capital is available to support future business plans, the firm's risk appetite and to meet regulatory requirements. The regulatory agenda continues to evolve and the Company remains well positioned to respond to change whilst maintaining a strong culture of client service.

Looking forward, the Company will continue to facilitate integration and co-location of staff of the Company with the UK branch of another MUFG subsidiary, The Bank of Tokyo Mitsubishi UFJ ("BTMU"). This initiative, detailed in the 2016 year-end Financial Statements, has further progressed during the current year, including the formal dual-hatting of certain employees. This integration supports achievement of the group vision of "one MUFG" brand supporting a broad product offering and improved revenue potential in a cost efficient manner.

Management retains a positive outlook as the Company continues to make progress against its strategic objectives and infrastructure change programme, as outlined in internal mid-term business plans. Management continue to identify opportunities to leverage MUFG's global franchise strength whilst efficiently utilising the Company's capital, infrastructure and staff resources within defined risk appetite parameters. Deepening relationships with our core clients and a focus on expanding the client coverage in partnership with BTMU sets firm foundations for the ongoing growth of the business.

Strategic Report (continued)

Business review and future development (continued)

The Board monitors the results of the Company by reference to various performance and risk based key metrics including:

- Revenue metrics: total operating income of £325.0 million (2016: £286.3 million) with a focus on quality of earnings and tracking against revenue plans
- Efficiency metrics: total operating expenses as a percentage of total operating income of 67% (2016: 72%) with a focus on efficient cost deployment
- Profitability metrics: return on equity ("ROE") calculated as profit attributable to owners of the company (refer to page 19), divided by the average of opening and closing total equity excluding Additional Tier 1 ("AT1"), of 7% (2016: 6%) with a focus on maximising ROE in the interests of shareholder returns
- Capital metrics: total capital requirements based on Pillar 1 requirements of £729.0 million (2016: £588.0 million) with a focus on optimising capital allocation and drivers of requirements
- Risk metrics: Total Value at Risk ("VaR"), as defined in the Business and Risk Management section, of £3.2 million (2016: £3.4 million) with a focus on tracking VaR.

Challenges and uncertainties

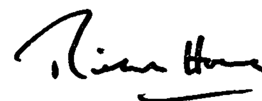
The Company faces a number of challenges and uncertainties in the normal course of its business. Operational risks are inherent in the Company's business activities and are covered in more detail under Business and Risk Management Policies on pages 6 to 16. Other uncertainties faced by the Company in the course of its business include: liquidity, funding and market risks; the valuation of financial assets and liabilities in volatile markets; exposure to macro-economic and geopolitical uncertainty; changes to regulatory rules regarding market practices and regulatory capital.

Following the outcome of the UK Referendum vote, it is clear that the political situation and hence the market outlook is less certain. MUS(EMEA) management has actively been considering the impact of Brexit on the business and has a contingency plan in place, including the setup of a subsidiary in the EU in 2018, to continue to provide services to EU clients. The aim of this contingency is to minimise the uncertainty arising from the manner of UK's exit from the EU and to ensure that the Company can continue to offer relevant and innovative solutions across Europe. Management is not aware of any specific issues faced by the Company, that are not faced by the rest of the financial services sector within the United Kingdom as a whole, and is maintaining communication with market peers. UK and appropriate EU regulators have been contacted and presented with interim analysis and planning.

The Company is exposed to fluctuations in the Japanese market through its debt issuance programme and its investment in high quality Japanese Government securities. The business activities of the ultimate parent company MUFG, whilst carried out on a global level, are focused on the Japanese market. The downgrade of Japanese debt, interest rate volatility and associated monetary and fiscal policy decisions, could impact the results of the Company. Management are fully aware of these risks and have plans in place to limit the impact to the Company.

Taking the above into consideration, including expected future profitability and continuing support from MUSHD, the Board believe it is reasonable to assume that the Company will have adequate resources in place to continue trading for the foreseeable future. As such, the financial statements have been prepared on the going concern basis.

By order of the Board



Richard House
Company Secretary
25 Ropemaker Street
London EC2Y 9AJ
2 March 2018

Directors' Report

The Directors present their annual report and financial statements for the year ended 31 December 2017.

Directors

The Directors during the year were as follows:

William Fall	Chairman (Independent)	
Takami Onodera	Non-Executive Director	(resigned 4 August 2017)
Diane Moore	Independent Non-Executive Director	
Stephen Jack	Independent Non-Executive Director	
Gordon Sangster	Independent Non-Executive Director	(appointed 26 September 2017)
Masamichi Yasuda	Non-Executive Director	
Masahiro Kuwahara	Non-Executive Director	
Akihiro Sugimura	Non-Executive Director	(appointed 4 August 2017)
David King	Chief Executive Officer	
Christopher Kyle	Chief Financial Officer	
Arthur Maycock	Chief Risk Officer	

Non-Executive Directors are employed by another MUFG company and undertake other roles within the group, in addition to their directorship of the Company. In accordance with the UK Corporate Governance Code's 2014 definition, the Independent Non-Executive Directors have been adjudged to be independent.

Chairman

William Fall continues his appointment as independent Chairman and Non-Executive Director. Mr. Fall plays a key role in a number of strategic initiatives relating to oversight of business strategy, client activity, culture and collaboration with other MUFG entities.

Directors' and officers' indemnities

The Company maintained insurance against liabilities for all Directors and officers of the Company during the financial year and at the date of this report.

Dividend and distributions

On 16 January 2017, the Directors approved the initial coupon payment of £728k on the AT1 capital issued on 15 December 2016 (refer to Note 20 for terms of the issuance).

On 15 July 2017, the Directors approved a coupon payment on the AT1 capital instruments of £4,418k.

On 15 January 2018, the Directors approved a coupon payment on the AT1 capital instruments of £4,273k. The amount has not been accrued in the results for the year ended 31 December 2017 as it was not due at that date.

No ordinary dividends were approved or paid during the year (2016: £ Nil).

Use of financial instruments

The trading and issuance of financial instruments is integral to the business activities of the Company. Information regarding the use of financial instruments is included within the Business and Risk Management Policies on pages 6 to 16.

Compensation

Certain employees' discretionary remuneration is deferred where the reward exceeds thresholds set by the Remuneration Committee, which meet the guidelines set out by the Prudential Regulatory Authority ("PRA"). Some of these deferrals take the form of Notional Stock Units ("NSU"), which track the performance of MUFG shares (refer to Note 6).

Employees

It is the policy of the Company to give full and fair consideration to applications for employment from disabled persons, to continue wherever possible the employment of members of staff who may become disabled and to ensure that suitable training, career development and promotion are encouraged.

Directors' Report (continued)

The Company places considerable value on the involvement of its employees, has continued to keep them informed on personnel policies or issues, matters affecting them as employees and on the various factors affecting the performance of the Company. This is achieved through formal and informal meetings, the Company intranet and regular internal communications. Employee representatives are consulted regularly on a wide range of matters affecting their current and future interests. These communications help to achieve a common awareness amongst employees of the financial and economic factors affecting the performance of the Company and the broader MUFG companies.

A Diversity and Inclusion working group has been established with the objective of maintaining and preserving our culture of high performance in a workplace that respects, appreciates and values individual differences. A formal Diversity and Inclusion Policy has been published internally, with employee demographics reviewed and emerging themes considered.

Corporate social responsibility

As a responsible business MUS(EMEA) has a focused Corporate Social Responsibility ("CSR") programme that aims to have a positive impact in the communities in which our business operates. Our CSR activities concentrate on supporting our local communities – in particular young people and the environment.

Through the Company's charity partnerships employees volunteer to use their skills and experience to support the community, maximising the positive impact on young people and the environment. The Company also supports charities through donations and continues to leverage employees' charitable activities through matched fundraising and "Give As You Earn" schemes. The Company's focus for 2018 will be to continue to promote a culture of integrity and social responsibility by maintaining the programme.

Disclosure of information to the auditor

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Company's auditor is unaware; and each Director has taken all the steps that they ought to have taken as a director to make themself aware of any relevant audit information and to establish that the Company's auditor is aware of the same information. This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to reappoint them will be proposed at the forthcoming Annual General Meeting.

By order of the Board

Richard House
Company Secretary
25 Ropemaker Street
London EC2Y 9AJ
2 March 2018

Statement of Directors' Responsibilities in Respect of the Strategic Report, Directors' Report and the Financial Statements

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 financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with IFRS as adopted by the European Union.

Under company law the Directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the company and of the profit or loss of the company for that period. In preparing these financial statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance, and
- make an assessment of the Company's ability to continue as a going concern.

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

The Directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

By order of the Board

Richard House
Company Secretary
25 Ropemaker Street
London EC2Y 9AJ
2 March 2018

Business and Risk Management Policies

Risk Management Framework

The Company maintains positions in financial instruments as an integral part of daily market activities. These positions are held as part of portfolios that are maintained and monitored by instrument or risk type. The risk appetite is set by the Board and individual trading areas are allocated risk limits based on a wide range of market factors and are required to maintain portfolios within those limits. As such they are responsible for maintaining hedges in the portfolios.

A more detailed explanation of risk strategy and factors is given below.

Committees and Corporate Structure

1. Board

The responsibility for risk management resides with the Board, with support from the Board Risk Committee ("BRC"). As part of the Company's business strategy, the Board considers the risks to which the Company is exposed, and specifies an appetite and management strategy for each of these risks. The primary financial, operational and reputational risks are defined and discussed in further detail in the following sections.

The Board has approved an enterprise-wide risk management framework for the Company which describes the Company's approach to risk appetite, strategy, governance, reporting and controls to ensure that risks taken are appropriately measured, monitored, reported, controlled and limited to the confines of the Company's risk appetite. The Board is ultimately responsible for reviewing the adequacy of the enterprise-wide risk management framework. The Directors consider that the framework currently in place is adequate.

2. Board Risk Committee

The objective of the BRC is to exercise oversight on behalf of the Board over the key risks facing the Company and to review and make recommendations to the Board on the Company's risk appetite and risk strategy, risk management framework (incorporating principles, policies, methodologies, systems, processes, procedures and people), and risk culture to ensure that it supports the Company's risk appetite.

As at 31 December 2017, the Committee comprised of the Independent Non-Executive Directors, including the Chair of the Board. The Committee is supported by the regular attendance of the Chief Risk Officer ("CRO"). Regulatory change and reviewing the Company's preparation to comply with new rules continued to be a key area for the Committee, including the requirements of the Market in Financial Instruments Directive II ("MiFID II"). Other topics focussed on by the Committee included: Risks arising from the integration of key business functions with BTMU; preparations and stresses arising from political changes such as the UK's negotiations over its departure from the EU; information security and cyber risk; internal assessments of the adequacy and projections for capital, liquidity and the Leverage Ratio; the overall risk appetite of the Company and the risk profile of each of the Company's business lines.

3. Risk structure and other committees

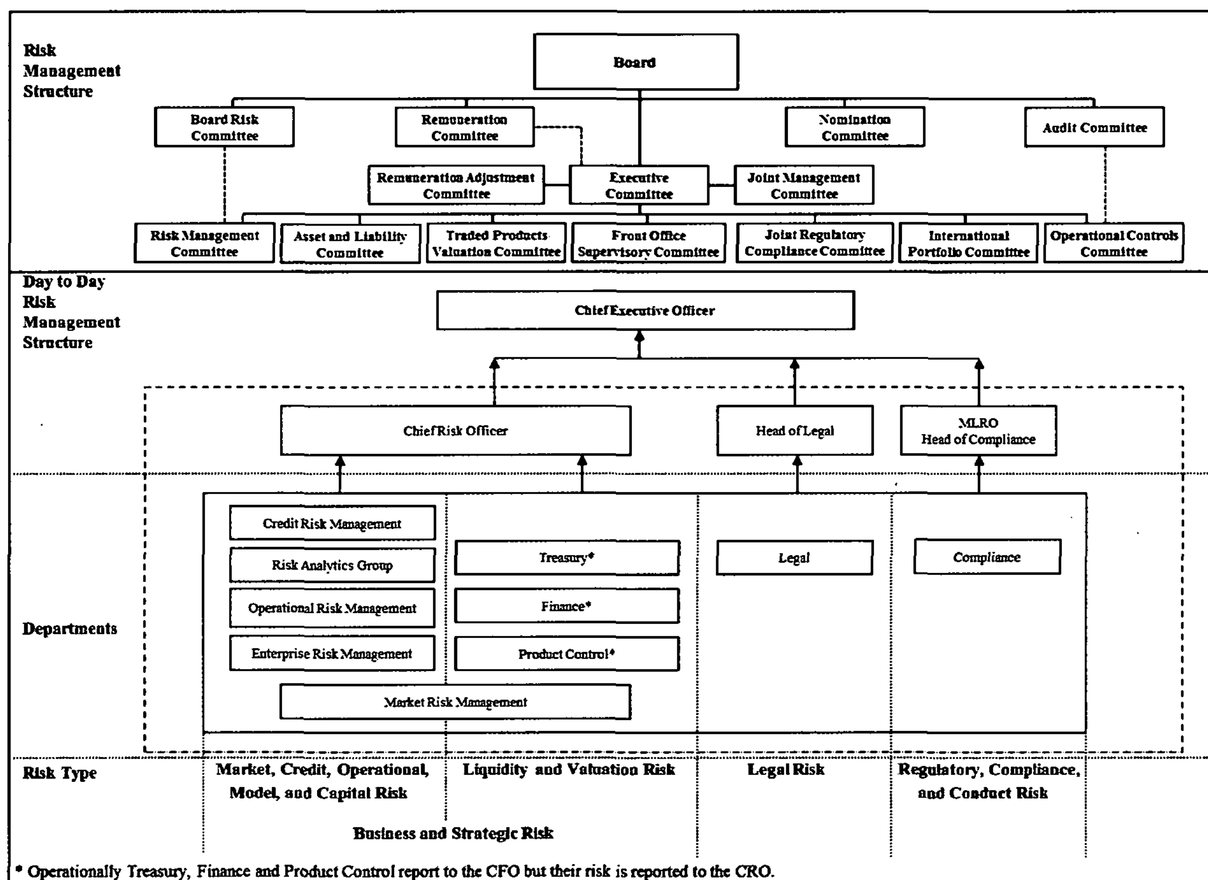
Day-to-day risk management of all risks, with the exception of compliance, conduct, legal and reputational risk, resides with the CRO, who reports directly to the Chief Executive Officer ("CEO") and the BRC. Market, credit, operational, and model risk are overseen by the Risk Management Committee ("RMC") supported by its underlying working groups.

Valuation risk is overseen by the Traded Products Valuation Committee ("TPVC"). Liquidity and capital risk is overseen by the Asset and Liability Committee ("ALCO"). Compliance, conduct and legal risk are overseen by the Joint Regulatory Compliance Committee. Day-to-day risk management of compliance risk and conduct risk resides with the Head of Compliance, who reports directly to the CEO. Legal risk management resides with the Head of Legal, who reports directly to the CEO. Reputational risk management resides with the CEO and the Executive Committee.

Each of these executive sub-committees report to the Executive Committee, which reports directly to the Board. In addition, the RMC reports to the BRC, via the CRO.

Business and Risk Management (continued)

The Company's risk committee and corporate structure as at 31st December 2017 is illustrated below:



Three Lines of Defence

The Company's governance of risk is based on the "Three Lines of Defence" approach:

1. Business Management – Front Office and functional support departments
   Department Heads and all Front Office staff are responsible for:
   - Managing the risks inherent in their business activities
   - Supervision, ensuring competence and training of their staff
   - Escalating risk issues to the Executive Committee, Joint Management Committee, RMC, ALCO, or the Operational Controls Committee ("OCC").

2. Challenge and Risk Control – Risk Departments and other control support departments
   - Independent of Front Office, led by the CRO, Chief Financial Officer ("CFO") and the Head of Compliance
   - Enable the Company to maintain a system of checks and balances
   - Escalate risk issues to the RMC, TPVC, ALCO, OCC and where appropriate to the Executive Committee
   - The Risk function and the RMC have a reporting line to the BRC, independent of the CEO.

3. Assurance – Internal Audit
   - Assurance role carried out by Internal Audit
   - Independent opinion to Senior Management and the Audit Committee of the Board
   - Objective appraisal of the adequacy and effectiveness of the internal control systems designed and installed by Senior Management and their remediation
   - Reports to Senior Management on whether the control systems are fulfilling, or are likely to fulfil, the control objectives of the Company
   - Independent reporting line to the Chair of the Audit Committee of the Board.

Risk Appetite

Central to the Company's risk management is a clear risk appetite, consistent with its business profile and plans, as well as a strong and independent review and challenge structure. This facilitates optimisation of risk/return and assists Senior Management to effectively control and coordinate risk taking across the business. The Company's risk appetite is specified by the Board through a number of metrics including capital, liquidity, earnings volatility, market, and credit risk. It is reviewed at regular meetings of the Board and reset annually as part of the Company's budget and planning process. The risk appetite is cascaded through the Company via the allocation of limits to front office departments and individual traders.

Business and Risk Management (continued)

Risk limits impose an upper constraint on the level of exposure to a particular factor or a combination of factors. Limits are imposed to express the Board and Senior Management's appetite for certain risk types and to facilitate prudent allocation of such risk appetite to individual risk takers or group of risk takers, taking client needs and revenue targets into consideration. These are set at the Company, business unit, department, and trader level and risk limits are monitored daily.

The establishment of the risk appetite is largely a top down process and is supplemented and reinforced by a bottom up approach to risk identification, the results of which are maintained in the Company's risk register.

The Company establishes and is subject to risk policies. These policies formalise the behaviours and standards expected in support of the risk culture. Policies are established across each primary risk type to formalise the processes by which business activities should fall within the appetite for each risk. Additionally, risk policies are established to ensure quality of risk measurement, risk monitoring, and appropriate avenues for escalation to occur.

The Company has established formal processes governing new business, complex transactions and new product mandates, which support the identification of any additional risk to the Company and ensure that the risks related to the proposal are within the risk appetite of the Company and has the support of the Company's risk management functions.

Capital Adequacy

The Company monitors its capital adequacy on an ongoing basis and conducts a formal annual Internal Capital Adequacy Assessment Process ("ICAAP") in which it assesses its risks, controls and capital.

The Board is involved in all the key elements of the ICAAP and approves the business and capital plans, Risk Appetite Statement, stress testing framework and preparation of the ICAAP document. The ICAAP process is closely aligned with the strategy setting and business planning process as well as the process for identification, measurement and control of those risks.

Stress testing is used to assess the impact of severe but plausible financial stresses on either individual or multiple risk factors and to determine appropriate capital buffers. The Company manages its risk and capital resources with the objective of maintaining a regulatory ratio comfortably in excess of the minimum capital resources required by the regulators.

Stress Testing

The Company has a stress testing framework that includes scenario stress testing (comprising macroeconomic and event stress testing based upon forward looking, historical and reverse stress testing), as well as single risk factor stress tests (which are designed to identify and quantify risk concentrations to particular risk factors). Results of stress testing are calculated at the Company level and also by department and business line, and reported regularly to Senior Management.

Risk Management by Risk Type

Market Risk

Market risk is the risk of losses from movements in market prices in the trading portfolio. The Company uses a variety of risk measures to quantify and control this risk, with the overall objective of ensuring that potential losses arising from market risk remain within the appetite set by the Board:

- Value at Risk ("VaR"), Stressed Value at Risk ("SVaR"), and Incremental Risk Charge ("IRC") measures provide aggregate indicators of potential losses, subject to stated confidence levels and holding periods
- Risk factor sensitivities measure the impact of moves in each risk factor, allowing concentrations of risk to be identified and controlled
- Stress testing is used to monitor and control the exposure of the portfolio to extreme moves in market rates and prices. A range of stress tests is run, covering exposures to relevant market factors and scenarios in various market conditions
- Stop loss and drawdown limits monitor actual losses at Company, business unit, department, and trader level.

The Company makes use of a range of internal models for the quantification of market risk.

VaR Modelling

The VaR of a trading book is an estimate of the potential loss on risk positions as a result of movements in market rates and prices over a specific time horizon and to a given confidence level.

The Company uses VaR methodologies to monitor the price risks arising from different trading books across portfolios. This is measured based on a 99% confidence level and a 1-day holding period.

Actual profit and loss outcomes are also monitored to test the validity of the assumptions made in the calculation of VaR. The VaR outputs are based on a full revaluation historical simulation model and a 2-year data window.

The Company additionally calculates SVaR using an appropriately stressed 1-year lookback period as required by regulatory rules.

VaR Backtesting

The Company carries out a daily comparison of end of day VaR measures to the 1-day change of the portfolio's value on the day the profit and loss figures are produced. In 2017 the number of occasions on which actual trading book outcomes exceeded the previous day's VaR was within the acceptable tolerances of the model.

Stressed VaR
The Company calculates SVaR based on inputs calibrated to historical data from a continuous twelve-month period of significant financial stress relevant to the Company's portfolio.

Risks Not In VaR
The Company calculates additional capital under its Risks Not In VaR framework for certain risk factors that are not fully captured in VaR.

Incremental Risk Charge
The Company calculates IRC which captures risk from the default and rating migration of non-securitised credit exposures in the trading book. The IRC is calculated daily and is included in regulatory capital calculations. IRC is calculated using a Monte Carlo model of portfolio rating migration and default. Risk is measured over a 1-year horizon to a confidence level of 99.9% and is calculated on current positions assuming that risk will be at similar levels throughout the year.

VaR considered in isolation has limitations which are listed below in further detail. The Company also uses a wide range of other risk limits, for example stop-loss limits, risk factor sensitivity limits or stress limits, to manage its exposures.

The Company's VaR has the following limitations:

- Calculations are based on historical data which may not be the best estimate of risk factor changes that will occur in the future
- In transforming historical data into future scenarios the Company makes assumptions that may not be the best estimate of how changes will occur in the future
- Focusing on the maximum loss that is expected to be incurred 99% of the time says little about the smaller losses that are expected to be incurred more frequently, or the larger losses in excess of VaR that are expected to be incurred 1% of the time
- VaR is generally based on calculations performed at the end of each business day. The end-of-day figure may not be representative of the figure at other times of the day.

The following table shows VaR figures for 2017 and 2016. The breakdown in terms of different risk factors is as described below. The "Close" column shows the VaR at the year end date. The "Average" column shows the average VaR measurement from each trading day in the year and the "Maximum" and "Minimum" columns show the highest and lowest VaR value in the year respectively. "Diversification benefit" is the difference between the simple sum of the VaRs for each risk factor, and the Company's overall VaR, which is based on the simultaneous modelling of all risk factors.

As at 31 December 2017	**Close £m**	**Average £m**	**Maximum £m**	**Minimum £m**
Interest Rate Curve Risk	1.5	2.1	3.8	0.7
Interest Rate Vega Risk	1.1	1.9	2.9	1.0
Asset Spread Risk	2.2	1.7	2.7	0.9
Currency Risk	0.6	0.8	1.8	0.2
Equity Price Risk	0.6	0.6	1.4	0.0
Equity Vega Risk	0.5	0.6	1.6	0.1
Inflation Risk	0.1	0.2	0.5	0.1
Basis Risk	1.8	2.0	3.1	1.1
Diversification benefit	-5.2	-6.4	n/a	n/a
Total VaR	**3.2**	**3.4**	**5.0**	**2.4**

As at 31 December 2016	**Close £m**	**Average £m**	**Maximum £m**	**Minimum £m**
Interest Rate Curve Risk	1.2	2.0	3.8	0.6
Interest Rate Vega Risk	2.0	2.5	5.0	0.6
Asset Spread Risk	1.7	1.1	3.3	0.6
Currency Risk	1.6	1.0	2.4	0.3
Equity Price Risk	1.3	0.7	2.5	0.1
Equity Vega Risk	0.7	0.7	1.7	0.2
Inflation Risk	0.4	0.3	0.6	0.1
Basis Risk	2.9	1.6	3.0	1.0
Diversification benefit	-8.4	-6.9	n/a	n/a
Total VaR	**3.4**	**3.0**	**5.0**	**1.7**

Interest Rate Curve Risk
The risk of losses arising from changes in market interest rates.

Interest Rate Vega Risk
The risk of losses arising from changes in the market price of interest rate options (i.e. implied rate volatility).

Asset Spread Risk
The risk of losses due to the market price of bonds and credit derivatives attributable to changes in such factors as perceived credit quality or liquidity, as distinct from price changes attributable solely to market interest rates.

Currency Risk
The risk of losses arising from changes in market FX rates, as well as the market prices of FX options (i.e. implied FX volatility).

Equity Price Risk
The risk of losses due to price movements in the equity market.

Equity Vega Risk
The risk of losses arising from changes in the market price of equity options (i.e. implied equity volatility).

Inflation Risk
The risk of losses arising from the changes in the market prices of inflation derivatives, or from price changes in inflation-linked securities attributable to inflation.

Basis Risk
The risk of losses arising from changes in market prices for cross currency basis, tenor basis, and other basis swaps in the interest rate market.

Credit Risk

Credit risk is the risk of loss resulting from client, issuer or counterparty default and arises on credit exposure in all forms, including settlement risk.

The Company manages its credit risks in accordance with policies originated and approved within the Company and endorsed by its parent company. Counterparty exposure is managed through a process of credit risk assessment, limit setting, exposure monitoring and exception reporting.

The Company assesses the default probabilities of individual counterparties by using a rating methodology incorporating external ratings, the market price of credit risk and internal fundamental analysis.

Day–to-day responsibility for the management of credit risk resides with the Credit Risk Management department, which is organisationally independent from the front office departments, and the Risk Analytics Group which is responsible for the design of new credit risk management models. Daily credit risk reports are prepared for Senior Management and trading departments using the Company's in house and vendor systems. Their objective is to:

- Identify, quantify, monitor and control credit risk exposure
- Provide sufficient, timely and relevant data of credit risk exposure by counterparty across all product classes and against each respective approved credit limit
- Maintain static data for all counterparties
- Produce timely credit risk reports as appropriate
- Mitigate credit risk by receiving collateral in accordance with the Company's Collateral Policy
- Provide credit portfolio monitoring and analysis.

On a monthly basis, Credit Risk Management reports the Company's total credit risk exposure to the RMC, including a review of large exposures, exposures to lower rated issuers and counterparties, and exposure to higher risk industry and country sectors. The RMC is also the forum where credit policies are reviewed and finally approved.

In addition to the RMC, a summary of the Company's credit risk exposure is also reported monthly to the BRC.

Credit exposure is normally measured on a net basis i.e. by taking account of received collateral and aggregating trades with both positive and negative values provided that a legally enforceable master netting agreement has been executed that permits close-out netting. To mitigate derivative counterparty credit risk, the Company has Credit Support Annexes in place with the majority of its counterparties and guarantee arrangements in place with members of MUFG; risk is managed net of these guarantees.

An analysis of the Company's credit exposures is included in Note 30.

Credit Concentration Risk

Credit concentration risk is the risk arising from an uneven distribution of exposures, through single name, sector or geographical concentration. The Company analyses the credit concentrations through its daily credit exposure reports. The Company's exposures are concentrated on Government bonds, the financial sector and exposures to Japanese markets and counterparties.

Liquidity Risk

Liquidity risk is the risk that the Company has insufficient resources to meet its financial obligations as they fall due. This risk could arise from both institution specific and market-wide events.

Oversight
The ultimate responsibility for liquidity risk management sits with the Board who sets the Company's liquidity risk appetite, which expresses the level of risk the Company chooses to take in pursuit of its strategic objectives. The Board mandate to the Executive Committee in respect of liquidity risk includes specification of liquidity stress testing, approval of business line unsecured funding limits, transfer pricing rates/policy and the contingency funding plan.

The Executive Committee has determined the powers and discretions delegated to the ALCO which meets monthly or on an ad-hoc basis (as appropriate) to:

- Review and define the funding and liquidity risk policy
- Monitor the Company's liquidity risk profile and review compliance with the Board approved liquidity risk appetite
- Oversee and review stress testing
- Measure, monitor and mitigate liquidity risk exposures for the Company
- Ensure that appropriate business incentives are maintained that reflect the cost and availability of liquidity through the Company's Fund Transfer Pricing ("FTP") process and unsecured funding limit allocation process
- Review critical liquidity risk factors and prioritise issues arising
- Determine the Company's funding plans and funding diversification strategy in light of business projections and objectives.

The Company uses a variety of quantitative and qualitative measures to monitor the adequacy of the Company's liquidity resources and to ensure an integrated approach to liquidity risk management. This framework incorporates a range of tools described below:

Internal Stress Testing
The Company's primary liquidity stress testing tool is the Maximum Cumulative Outflow, which is designed to capture all material drivers of liquidity risk (both on and off balance sheet) and to evaluate the subsequent liquidity outflow in order to determine the size of liquidity resources needed to navigate the stress event. The model has been developed using scenarios based on market practice, regulatory requirements and past experience in stressed market conditions. It is based on a synthesis of scenarios categorised as baseline (reflective of normal business conditions), systemic (refers to a market-wide liquidity event) and combined (analogous of a combined market and Company specific stress event). Stress testing is conducted on both an aggregated currency basis and by material individual currency.

Fund Transfer Pricing
The Company seeks to align its liquidity risk appetite with the strategic objectives of the business through regulating the demand for liquidity and allocating the cost of liquidity on the basis of unsecured funding usage and underlying liquidity requirements. The ALCO is responsible for the FTP policy framework, and Treasury is responsible for the day to day application of the FTP framework. The cost of funding is allocated to businesses on the basis of the funding requirements to finance current inventory positions and ongoing business activities. The cost of liquidity reserved to cover contingent liquidity outflows is also allocated to the business – this includes liquidity reserved to cover regulatory liquidity requirements.

Funding Plan
The balance sheet projection process balances aggregate business line requests for unsecured funding against Treasury's assessment of the projected balance sheet, funding requirements and capacity for the Company to raise unsecured financing. The ALCO will review and approve funding plans including allocation of funding limits to business lines. This ensures that business activities do not impose an unknown strain on the Company's ability to source adequate liquidity in normal business conditions, and allows Treasury to plan and sustain appropriate levels of liquidity in anticipation of business line funding usage. As part of funding liquidity risk monitoring, Treasury looks at the short and long term currency mismatch horizons in accordance with the Board's guideline.

Liquid Asset Buffer
The liquidity requirement is quantified through both the internal stress testing framework and regulatory requirement. The Company holds its liquidity portfolio in a stock of high quality government bonds and bonds issued by multi-lateral development banks, local government and agency issuers. The liquidity portfolio is held on an unencumbered basis without restrictions on rehypothecation and with full Company legal ownership. The investment criteria for the liquidity portfolio are approved by ALCO with risk limits imposed and monitored by Market Risk Management.

Business and Risk Management (continued)

Contingency Funding Plan
The Contingency Funding Plan ("CFP") allows senior management to identify internal and external triggers indicative of a stress event, and to initiate the most effective response for stabilising and mitigating liquidity risk exposures through clear operational plans, clearly defined decision making responsibilities and effective communication with both internal and external stakeholders. The CFP also specifies the means through which additional funding should be sourced during a period of heightened liquidity concern.

The Company also maintains detailed recovery plans which consider actions to facilitate recovery or an orderly resolution from a severe stress.

Liquidity Stage Assessment
The principal assessment framework within the Funding Liquidity Risk Management Policy is the liquidity stage assessment. This is a formal assessment of the external environment affecting the Company and other companies within the MUSHD Group.

The liquidity stage is determined by an evaluation of the availability of funding and is monitored through a combination of early warning indicators, the Company's internal stress testing and compliance with regulatory liquidity requirements. Elevation of the liquidity stage is specifically linked to activation of the CFP, which provides a range of mitigating actions to be taken. Such actions are taken following consideration of any relevant market, economic or client impact. In the event the liquidity stage is elevated, formal approval is required from the ALCO, which will in turn escalate and sanction actions as appropriate. Monitoring of the liquidity stage is conducted at Company and MUSHD level on an on-going basis. Any elevation of liquidity stage risk at the MUSHD level is deemed to represent a worsening of conditions that would impact the Company too. The Funding Liquidity Risk Policy identifies general contingency actions to be taken by departments at each stage.

Asset Encumbrance
Asset encumbrance arises from collateral pledged against secured funding and other collateralised obligations. Due to the nature of its business the Company funds a portion of debt securities via repurchase agreements and other similar secured borrowing. Additionally debt securities and cash are provided to meet initial and variation margin requirements from central clearing counterparts and margin requirements arising from derivative and repurchase agreements.

The Company monitors the mix of secured and unsecured funding sources and seeks to efficiently utilise collateral to raise secured funding and meet other collateralised obligations.

Regulation
The Company assesses liquidity adequacy as part of its Internal Liquidity Adequacy Assessment Process that it submits to the PRA. The Company's compliance with prevailing regulatory liquidity requirements including the Liquidity Coverage Ratio are complemented by the internal stress testing framework. The Company manages its liquidity prudently, holding its Liquid Asset Buffer well in excess of the regulatory requirement.

Capital Risk

Capital risk is the risk that the Company has insufficient capital resources to meet the capital requirements that are incurred through execution of the business plan.

The Company aims to manage and control its exposure to Capital Risk through its policies and procedures with the objectives of:

- Holding sufficient capital resources to support the risks in which the Company engages
- Identifying an appropriate capital plan to ensure that this objective is maintained over the three year business plan horizon
- Managing the relative proportions of the constituent parts of capital resources such that the Company meets these objectives in an efficient manner.

The ALCO has primary responsibility for overseeing the Company's capital management. The RMC has secondary responsibility due to the direct impact of market, credit, operational and other risks on capital requirements and capital resources. The Company measures key capital sensitivities and analysis of drivers of change in capital adequacy which are regularly reported to the ALCO and the RMC.

The Company assesses capital risk against minimum regulatory requirements and internal targets at Company level, supported by assessments of capital requirements at business level against internal targets. Capital risk assessments are reported regularly to the ALCO and the RMC. Capital risk reports are circulated to senior management daily and are discussed at Board and Committee level.

The Company determines and maintains a capital planning buffer to reduce the risk of having to raise capital or reduce business at short notice. The Company's objective is to manage capital to withstand severe but plausible stresses without the need to significantly alter the business. This capital planning buffer is determined on the basis of appropriate stresses to the Company's business.

Model Risk

Model risk is the potential for loss arising from decisions based on incorrect or misused model outputs and reports.

The firm manages model risk by having a segregation of duties between model development and validation of the model. There are governance working groups that oversee the models used by the Company. In the case of risk models, the Model Oversight Working Group ("MOWG"), which reports to the RMC, is responsible for reviewing the output of ongoing validation and for model performance. The Valuations Working Group "VWG" oversees the use of pricing models. The independent validation of models is performed by the Independent Risk Validation function which is part of the Company's Internal Audit department and has membership on the MOWG and the VWG.

Operational Risk

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk.

The Company manages and controls its exposure to Operational Risk through its policies and procedures, which are designed to ensure that it:

- Mitigates the risk of exposure to fraud
- Processes transactions correctly, accurately and on a timely basis
- Protects the integrity and availability of information processing facilities, infrastructure and data
- Maintains the confidentiality of its client information
- Employs appropriate numbers of skilled staff and complies with relevant employment laws and regulations
- Establishes workplace environments that are safe for both employees and visitors
- Reduces both the likelihood of an incident occurring and the impact should an incident occur.

The Company employs The Standardised Approach ("TSA") for calculating its Pillar 1 Operational Risk Capital Requirement. The Company is committed to adopting leading industry practices for managing and measuring Operational Risk, and has also developed a primarily scenario based capital model to determine whether it should hold any additional capital for Operational Risk.

Operational Risk Management Framework

In order to facilitate the management of Operational Risk, the Company sub-divides it into the seven Basel II categories, i.e.:

1. Execution, delivery and process management
2. Clients, products and business practices
3. Internal fraud risks
4. External fraud risks
5. Employment practices and workplace safety
6. Business disruption and systems failures
7. Damage to physical assets.

The Operational Risk Management framework is defined within the Company's policies and detailed standards, and comprises of the following key elements:

- Risk appetite: The Company has defined its Operational Risk Appetite in both quantitative and qualitative terms, reflecting both the financial and non-financial impacts that can arise from operational risk
- Self-assessments: Managers within the Company assess the effectiveness of their controls at mitigating the key operational risks, relative to the Company's appetite
- Key control attestations: Managers confirm regularly that their key controls have operated correctly
- Scenario analysis: The Company uses scenario analysis to assess the risks of extreme but plausible events
- Key risk & control indicators: The Company uses metrics to monitor its operational risk profile and to alert management when risk levels exceed acceptable ranges
- Incidents & losses: The Company systematically collects details of both operational risk losses (or gains) above a certain threshold and details of incidents, even if they have not led to losses (or gains) and root cause analysis where applicable
- Remedial actions: Progress in completing remedial actions is tracked and reported
- Reporting: The operational risk function and management uses reports to understand, monitor, manage and control operational risks
- Insurance policies: As part of its risk management approach, the Company uses insurance to mitigate the impact of some operational risks
- Training: Staff are required to undertake annually mandatory on-line operational risk awareness training.

The Company has a dedicated Operational Risk Management function. Issues of significance are escalated to the OCC, which meets on a monthly basis and is attended by members of Senior Management and heads of the control functions.

Pension Risk

Pension risk is the risk that there is a shortfall in the value of the assets of the defined benefit pension scheme relative to its liabilities. The main risk is that the assets that the pension scheme holds decline significantly and there is no offsetting change in liabilities, or that the liabilities increase with no offsetting increase in the assets.

The Company's defined benefit pension scheme was closed to new members on 2 July 1999. The assets held are not an exact match to the liabilities. A mandatory actuarial valuation of the fund is carried out every three years for the pension trustees. The Statement of Funding Principles of the scheme requires a recovery plan to eliminate any funding deficit over the next 10 years or sooner. The scheme was closed to future accrual on 31 January 2011. This action limited the future growth of the estimated liabilities of the defined benefit scheme. The Company calculates its pension risk on an annual basis as part of its ICAAP process and holds capital to mitigate against the possibility of a material deficit in its pension fund.

Further details on the Company's pension scheme can be found in Note 7.

Business Risk

Business risk is the sensitivity between expected revenues and expected costs. It is a measure of how easily the cost base can be managed in relation to lower than expected revenues. The risk of doing business is categorised as the volatility of the business planning forecast compared to the realised revenue which is dependent on the market environment.

Strategic Risk

Strategic risk is the risk of loss that may arise from the pursuit of an unsuccessful business plan including insufficient diversification of revenue sources. Strategic risk is a necessary consequence of doing business and covers a number of financial risk types. Strategic risks are generally longer term risks whereas shorter term risks will usually be captured as part of business risk. The Company's primary approach to the management of strategic risk is through its business planning processes which highlight the key dependencies of its strategy, which allows for the assessment of strategic risk at the point that the strategy is devised and agreed. The Company's programme of qualitative reverse stress testing is intended to focus on key strategic risks, identifying scenarios that could lead to their realisation as well as contingent actions that could be taken to address their emergence and mitigate the impact of the strategic risk being realised.

The Company's strategic risks also include potential impacts arising from the Company's relationship with its stakeholders and its relationship with MUFG. These risks include but are not limited to ongoing group support, maintenance of satisfactory relationships with key regulators, continued ability to meet core client demands, and the ability to attract and retain high quality staff.

Compliance Risk

Compliance risk is the risk of damage to the Company by failing to comply with financial services regulations, rules, guidelines, industry codes of conduct, organisation standards, professional ethics, Board and Senior Management standards or guidelines and other codes of conduct applicable to its business activities.

The Company's businesses are managed to achieve alignment between compliance risk profile and compliance risk appetite. Risk appetite is clearly defined and reflects the Company's strategy and values. Decision making is based on a thorough understanding of compliance risks, supported by robust analytics and measurement capabilities.

The Company maintains a governance structure that ensures appropriate management, oversight and assurance of significant risks and associated mitigation strategies, including, a compliance function with sufficient authority, stature, independence, resources and access to the Board. Accountability for compliance is shared by groups across the Company with front office and back office departments who own their respective compliance risks. The Compliance function is accountable for oversight of compliance controls; and the Internal Audit function accountable for providing independent assurance. The Company's compliance and internal control infrastructures evolve with changes to its risk profile, including its growth, and to the external regulatory landscape.

Conduct Risk

Conduct risk is the risk of damage on the Company's corporate value as a result of negative impact on public benefit, effective competition, market integrity or customer protection due to the inappropriate execution of our business activities through failure to comply with laws and regulations, breach of a social norm, improper business or market practice or lack of client's viewpoints.

Business and Risk Management (continued)

Effective identification and management of Conduct Risk is a key aspect of the Company's future success. Appropriate and demonstrable conduct risk management is not only an expectation of the regulators, it will additionally promote enhancement of the relationships the Company has with its clients. The Company has implemented a Conduct Risk Management Framework in response to regulatory demands for firms to efficiently identify, document and manage their conduct risks through an auditable process. Individual steps were previously in place but are now consolidated under the framework as follows:

- Compliance policies, front office desk procedures and a conduct risk operating framework and strategy
- A conduct risk appetite which defines the amount and type of conduct risk that the Board are willing to seek, accept or tolerate in order to achieve the firms' strategic objectives and business plan
- An operational framework to support the continuous process of conduct risk identification and assessment
- A formal compliance monitoring programme to review the effectiveness of key controls to mitigate potential conduct risk exposure
- Production and analysis of conduct risk management information
- Company-wide conduct risk training and awareness programme.

Legal Risk

Legal risk is the risk of loss or damage to the firm by failing to comply with any laws, regulations or contractual obligations applicable to its business activities or failure to take appropriate steps to manage legal claims or actions.

The Company manages legal risk by compliance with all applicable laws and regulations and promoting honesty and integrity by all staff. It seeks to promote prudent business growth and profitability through the rigorous control of legal and regulatory risks in support of the wider objectives of the Company. The Company has an established permanent Legal function that is independent of business activities and has sufficient resources to carry out its role including:

- Identification of the main legal and regulatory risk issues affecting the business, recommending how these will be managed and, where appropriate, elevating residual risks to the relevant front office department, risk management department or the Board and its sub-committees
- Identifying and advising on legal and regulatory change and its impact on the business and assisting with scoping and implementation of mitigating systems, controls and infrastructure
- Managing legal and regulatory risk through due diligence, review of contracts and transactions, negotiation of transaction documentation and the management of all legal and regulatory actions.

Reputational Risk

Reputational risk is the risk of loss arising from events that damage the reputation of the Company or the Group. It is usually a secondary risk which exacerbates the loss from another risk type. The Company's business is dependent on its reputation and it will impact its performance should it deteriorate. The Company has a Reputational Risk Framework, policy and controls to mitigate the impact and reduce the likelihood of reputational incidents.

Such incidents can occur in any type of risk from market through to operational, or from external risks over which the Company has no direct control. The Reputational Risk Management Policy sets out how the risk of reputational events is managed.

Status of Regulatory Capital Resources

The Company's regulatory capital resources are assessed under the Capital Requirements Regulation and the Capital Requirements Directive IV. The Company's capital consists of Tier 1 – retained earnings, share capital and AT1 instruments, and Tier 2 – subordinated debt which is fixed term and denominated in Japanese Yen.

The Company manages its risk profile and its capital resources with the objective of maintaining a capital ratio in excess of the Capital Resources Requirement for its risk profile at all times. The management of the Company's capital is carried out under the principle that it should not unexpectedly need to raise new capital or significantly reduce its risk taking in order to meet its capital management objectives.

The Company has fulfilled its capital requirements at all times during the year.

Business and Risk Management (continued)

The Company's capital resources, Pillar 1 capital requirements and capital ratios for 2017 and 2016 are shown in the table below:

	At 31 Dec 2017	At 31 Dec 2016
	£m	£m
Total Common Equity Tier 1 Capital after Deductions	1,058	1,009
Additional Tier 1 Capital after Deductions	307	302
Total Tier 2 Capital after Deductions	290	259
Total Capital Resources	**1,655**	**1,570**

	At 31 Dec 2017	At 31 Dec 2016
	£m	£m
Credit Risk (including Concentration Risk)	404	359
Market Risk	278	193
Operational Risk	47	36
Total Capital Requirements	**729**	**588**

	At 31 Dec 2017	At 31 Dec 2016
	%	%
Common Equity Tier 1 Ratio (Common Equity Tier 1 / Risk Weighted Assets)	11.6	13.7
Tier 1 Ratio (Tier 1 / Risk Weighted Assets)	15.0	17.8
Total Capital Ratio (Total Capital / Risk Weighted Assets)	**18.1**	**21.3**

Further details of the Company's capital requirements are included within the Company's Pillar 3 disclosure which is published on the Company's website.

Audit Committee

The Audit Committee meets at least four times a year and is comprised of five non-executive directors and is chaired by Stephen Jack. At least one of the members is deemed to have recent and relevant financial experience and all the members have strong backgrounds in financial services. The Audit Committee has responsibility for providing the Board with assurance on the effectiveness of the internal control and risk management systems, the integrity of financial reporting, the performance of the Internal and External Auditors, compliance with regulatory requirements and the reliability of the Company's auditing, accounting and financial reporting processes generally.

Over the past year, the Audit Committee has: reviewed and recommended the financial statements to the Board after considering the work done by the External Auditor and reviewing matters of materiality and items which because of their complexity require estimation or judgement by management; approved an Internal Audit plan and the resources of this function; considered reports and recommendations from Internal Audit and management's responses to these; reviewed Compliance's financial crime monitoring programme, whistleblowing procedures and other relevant regulatory reporting requirements; received reports from the Operational Risk function; reviewed the External Auditor's management letter and approved non-audit work carried out by the External Auditor. The Committee also reviews reports from the Regulatory Compliance Committee (which became the Joint Compliance Committee during the course of the year), and the Operational Controls Committee.

The Internal and External Auditors attend all meetings of the Committee. In addition, members of senior management are regularly invited to committee meetings in order to discuss reports, recommendations and action plans. The Chair is responsible for reporting on the work, findings and recommendations of the Committee to the Board.

The Audit Committee carries out an annual assessment of its own performance drawing upon the views of members and regular attendees. Steps are taken to address any significant points for improvement. The Committee also reviews the performance of the Internal and External Auditors on an annual basis.

The Audit Committee is responsible for the appointment of the external auditor and as such appointed Deloitte LLP in 2014. The Committee also considers the fees of the External Auditor and recommends these to the Board.

Independent Auditor's Report To The Members Of MUFG Securities EMEA plc

Report on the audit of the financial statements

Opinion

In our opinion the financial statements:

- give a true and fair view of the state of the company's affairs as at 31 December 2017 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements of MUFG Securities EMEA plc (the 'company') which comprise:

- the income statement;
- the statement of comprehensive income;
- the balance sheet;
- the statement of changes in equity;
- the cash flow statement;
- the statement of accounting policies; and
- the related notes 1 to 32.

The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in respect of these matters.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements
Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at: www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Use of our report
This report is made solely to the company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006
In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared are consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report and the directors' report.

Matters on which we are required to report by exception
Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- 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; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

We have nothing to report in respect of these matters.

Caroline Britton FCA (Senior statutory auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom

2 March 2018

Company income statement

For the year ended 31 December	Notes	2017 £'000	2016 £'000
Interest income	2	20,926	29,755
Interest expense	3	(4,433)	(12,769)
Net interest income		**16,493**	**16,986**
Fees and commissions income		74,021	73,149
Fees and commissions expense		(18,506)	(15,710)
Net fees and commissions income		**55,515**	**57,439**
Trading income		**250,896**	**203,890**
Net investment income		**2,050**	**7,950**
Total operating income		**324,954**	**286,265**
Administrative expenses	4	(198,874)	(192,136)
Amortisation of intangible assets	13	(14,914)	(12,815)
Depreciation of property, plant and equipment	14	(3,067)	(2,564)
Total operating expenses		**(216,855)**	**(207,515)**
Profit on ordinary activities before taxation		**108,099**	**78,750**
Taxation	8	(28,276)	(18,851)
Profit attributable to owners of the company		**79,823**	**59,899**

The above results are derived from continuing operations of the business.

Company statement of comprehensive income

For the year ended 31 December	2017 £'000	2016 £'000
Profit after tax	79,823	59,899
Other comprehensive income / (loss) from continuing operations:		
Available for sale reserve		
Net gains from changes in fair value	2,562	13,447
Net (gains) transferred to net profit	(2,544)	(7,950)
Taxation	17	(1,408)
Cash flow hedging reserve		
Net gains from changes in fair value	765	436
Net (gains) / losses transferred to net profit	(416)	258
Taxation	(87)	(171)
Total comprehensive income that may be recycled to profit or loss	80,120	64,511
Other comprehensive income / (loss) not recycled to profit or loss		
Actuarial gains / (losses) in retirement benefit schemes	16,047	(25,072)
Taxation	(4,253)	6,104
Total other comprehensive income / (loss)	11,794	(18,968)
Total comprehensive income for the year attributable to owners of the company	**91,914**	**45,543**

Company balance sheet

As at 31 December	Notes	2017 £'000	2016 £'000
ASSETS			
Cash and balances at central banks		976,430	975,454
Trading portfolio financial assets	10	8,458,660	5,359,009
Derivative financial instruments	11	13,445,575	19,296,980
Reverse repurchase agreements		22,459,995	42,384,371
Securities sold not delivered		985,285	1,202,543
Equity finance assets		488,261	485,331
Cash collateral on securities borrowed		6,468,603	7,824,309
Cash collateral paid to derivative counterparties		2,528,987	2,474,924
Loans and advances to banks		130,494	200,066
Financial instruments available for sale	12	818,739	1,757,381
Deferred tax asset		18,396	32,040
Intangible assets	13	65,793	50,172
Property, plant and equipment	14	17,353	13,297
Other assets	15	255,804	373,470
Total assets		**57,118,375**	**82,429,347**
LIABILITIES			
Deposits by banks		88,311	72,392
Trading portfolio financial liabilities	16	5,767,847	5,546,702
Derivative financial instruments	11	11,763,396	18,397,176
Repurchase agreements		21,990,927	41,936,030
Securities bought not delivered		916,459	1,396,090
Cash collateral on securities lent		1,772,714	444,514
Cash collateral received from derivative counterparties		7,606,270	7,853,174
Financial liabilities designated at fair value	17	4,665,013	4,563,537
Other liabilities	18	725,408	466,760
Subordinated liabilities	19	290,038	309,151
Total liabilities		**55,586,383**	**80,985,526**
EQUITY			
Equity instruments	20	1,317,590	1,317,590
Other reserves		2,049	1,752
Retained earnings		212,353	124,479
Total equity		**1,531,992**	**1,443,821**
Total liabilities and equity		**57,118,375**	**82,429,347**

Company Number: 1698498

The financial statements on pages 19 to 53 and business and risk management policies on pages 6 to 16 were approved by the Board of Directors and authorised for issue on 2 March 2018 and signed on its behalf by:

David King
Chief Executive Officer
2 March 2018

Company statement of changes in equity

	Share capital £'000	Additional Tier 1 capital £'000	Available for sale reserve £'000	Cash flow hedging reserve £'000	Retained earnings £'000	Total equity £'000
2016						
Balance 1 Jan 2016	1,010,611	-	(2,639)	(221)	83,548	1,091,299
Profit after tax	-	-	-	-	59,899	59,899
Issue of equity instruments	-	306,979	-	-	-	306,979
Available for sale investments	-	-	4,089	-	-	4,089
Cash flow hedges	-	-	-	523	-	523
Actuarial loss	-	-	-	-	(18,968)	(18,968)
Balance 31 Dec 2016	**1,010,611**	**306,979**	**1,450**	**302**	**124,479**	**1,443,821**
2017						
Balance 1 Jan 2017	1,010,611	306,979	1,450	302	124,479	1,443,821
Profit after tax	-	-	-	-	79,823	79,823
AT1 coupon	-	-	-	-	(3,743)	(3,743)
Available for sale investments	-	-	35	-	-	35
Cash flow hedges	-	-	-	262	-	262
Actuarial gain	-	-	-	-	11,794	11,794
Balance 31 Dec 2017	**1,010,611**	**306,979**	**1,485**	**564**	**212,353**	**1,531,992**

Company cash flow statement

For the year ended 31st December	Note	2017 £'000	2016 £'000
Reconciliation of profit before tax to net cash flows from operating activities			
Profit before tax		108,099	78,750
Adjustment for non-cash items:			
Depreciation and impairment of property, plant & equipment		3,067	2,564
Amortisation and impairment of intangible assets		15,527	12,815
Net loss on disposal of property, plant and equipment and intangible assets		180	3,938
Actuarial gain / (loss) on pension		11,794	(18,968)
Changes in operating assets and liabilities:			
Net (increase)/decrease in trading portfolio financial assets / liabilities		(2,878,506)	2,350,257
Net (increase)/decrease in derivative financial instruments		(782,374)	332,255
Net (increase)/decrease in securities bought / sold not delivered		(262,373)	885,683
Net decrease/(increase) in reverse repurchase agreements		19,924,376	(14,266,912)
Net (decrease)/increase in repurchase agreements		(19,945,103)	11,713,592
Net decrease/(increase) in loans and advances to banks		69,572	(63,584)
Net decrease/(increase) in cash collateral for securities and derivatives		2,382,939	(1,113,033)
Net decrease/(increase) other assets		128,378	(286,701)
Net increase/(decrease) in other liabilities		251,881	(43,470)
Corporation tax paid		(21,509)	(2,122)
Net cash used in operating activities		**(994,052)**	**(414,936)**
Purchase of property, plant and equipment		(7,159)	(3,017)
Purchase of intangible assets		(31,293)	(16,959)
Purchase of available for sale investments		(1,349,107)	(3,151,525)
Proceeds from sale or redemption of available for sale investments		2,287,749	3,510,334
Other cash inflows/(outflows) associated with investing activities		297	4,612
Net cash from investing activities		**900,487**	**343,445**
Issue of equity instruments - AT1		-	306,979
Proceeds from financial liabilities designated at fair value		8,712,851	4,507,779
Repayments of financial liabilities designated at fair value		(8,611,375)	(3,576,478)
Proceeds from drawdown of subordinated debt		-	309,117
Repayments and redemption of subordinated debt		(19,113)	(666,077)
Distributions paid to holders of AT1 capital (net)		(3,744)	-
Net cash from financing activities	9	**78,619**	**881,320**
Net (decrease) / increase in cash and cash equivalents		**(14,945)**	**809,829**
Opening cash and cash equivalents		903,062	93,233
Net cash increase		39,977	783,217
Foreign exchange		(54,921)	26,612
Closing cash and cash equivalents	9	**888,118**	**903,062**

Notes on Financial Statements

1 Accounting policies

Basis of preparation of company accounts

The financial information includes the financial statements of the Company for the year ended 31 December 2017. The financial information has been prepared under the historical cost convention modified by the revaluation to fair value of certain positions, and in accordance with International Financial Reporting Standards (IFRS) as adopted by the European Union and with the Companies Act 2006.

The financial statements have been prepared on a going concern basis due to expected future profitability and continuing support from MUSHD. The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the Strategic Report on pages 1 to 2. The financial position of the Company, its liquidity position and borrowing facilities are described through the financial statements beginning on page 19. In addition, the Business and Risk Management Policies on pages 6 to 16 include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; and various forms of risk.

The Company has considerable financial resources together with long-term support from MUSHD; as evidenced by additional capital raised during the comparative period, and contracts with both a broad range of customers and financial institutions across different geographic areas. As a consequence, the Directors believe that the Company is well placed to manage its business risks successfully despite the current uncertain global economic outlook. The Directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. Thus they continue to adopt the going concern basis in preparing the annual financial statements.

Use of estimates and assumptions

The preparation of financial information requires the use of estimates and assumptions about future conditions. The use of available information and the application of judgement are inherent in the formation of estimates; actual results in the future may differ from estimates upon which financial information is prepared. The Company believes that the critical accounting policies where judgement is necessarily applied are those which relate to the valuation of financial instruments (refer to Note 23), estimates of future cash flows or economic utility of assets which drive the impairment assessment of those assets not carried at fair value through profit and loss, assumptions included in the actuarial valuation of the defined benefit pension scheme (refer to Note 7) and recognition of deferred tax assets (refer to Note 8). See below for further comments on fair value measurement of financial assets and liabilities.

The recognition of a deferred tax asset relies on an assessment of the probability and sufficiency of future taxable profits, future reversals of existing taxable temporary differences and ongoing tax planning strategies. The most significant judgements relate to expected future profitability.

Trading assets and trading liabilities

Long and short positions in debt (bonds, pass through notes and asset backed securities) and equity securities, which have been acquired or incurred principally for the purpose of selling or repurchasing in the near term or which are part of a portfolio of identified financial instruments that are managed together and for which there is evidence of a recent actual pattern of short-term profit taking, are classified as held for trading. Such financial assets or financial liabilities are recognised initially at fair value, with transaction costs taken to the income statement, and are subsequently remeasured at fair value. All subsequent gains and losses from changes in the fair value of these assets and liabilities together with related interest income, interest expense and dividends, are recognised in the income statement within trading income as they arise. Financial assets and financial liabilities are recognised using trade date accounting.

Loans and receivables

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and receivables are initially recognised at fair value including direct and incremental transaction costs. They are subsequently valued at amortised cost, using the effective interest rate method, less any impairment.

Available for sale

Available for sale ("AFS") investments are non-derivative investments that are not designated as another category of financial asset and are carried at fair value. These securities are recognised using trade date accounting.

Interest income is recognised in the income statement using the effective interest method. Dividend income is recognised in the income statement when the Company becomes entitled to the dividend. Foreign exchange gains or losses on AFS debt security investments are recognised in net trading income. Other fair value changes are recognised directly in shareholder's equity within the AFS reserve until the investment is sold or impaired, at which time the balance in equity is recognised in the income statement.

1 Accounting policies (continued)

Financial instruments designated at fair value

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated by management. The Company may designate financial instruments at fair value when doing so results in more relevant information due to the following:

- It eliminates or significantly reduces valuation or recognition inconsistencies that would otherwise arise from measuring financial assets or financial liabilities, or recognising gains and losses on them, on different bases. Under this criterion, the main class of financial instruments designated by the Company includes medium term note issues and money market loans and deposits. The return on certain instruments has been matched with derivatives. An accounting mismatch would arise if the debt securities and money market transactions were accounted for at amortised cost, because the related derivatives are measured at fair value with movements in the fair value taken through the income statement. By designating these assets and liabilities at fair value, the movement in their fair value will also be recorded in the income statement.
- Groups of financial assets, financial liabilities or combinations thereof are managed and their performance evaluated, on a fair value basis in accordance with a documented risk management or investment strategy, and information about groups of financial instruments is reported to management on that basis.
- Certain financial instruments contain one or more embedded derivatives that significantly modify the cash flows resulting from those financial instruments.

The fair value designation, once made, is irrevocable. Designated financial assets and financial liabilities are recognised on trade date, when the Company enters into contractual arrangements with counterparties. Measurement is initially at fair value with transaction costs taken directly to the income statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in the income statement.

Repurchase and resale agreements

Securities which have been sold subject to an agreement to repurchase remain on the balance sheet and a liability based on the net present value of the associated future cash out flows is recorded within liabilities. Securities acquired in purchase and resale transactions are not recognised on the balance sheet and an asset based on the net present value of the associated future cash receipts is recorded within assets.

Certain transactions which are managed by the Treasury business are recorded as loans and receivables (reverse repurchase agreements) or liabilities at amortised cost (repurchase agreements). As such, the balances recorded in assets and liabilities are subsequently remeasured only to reflect the accrual of interest or impairment.

All other sale and repurchase and reverse repurchase agreements are treated as trading instruments. As such, the balances recorded in assets and liabilities are subsequently remeasured at fair value. Gains and losses from changes in the fair value of the associated cash flows are recognised in the income statement as they arise. Assets and liabilities are offset and the net amount reported on the balance sheet when there is a legally enforceable right to offset the recognised amounts and there is an intention to settle on a net basis.

Issued debt – financial liability vs equity classification

Issued financial instruments or their components are classified as equity when there is no contractual obligation to transfer cash, other financial assets or issue a variable number of the Company's own equity instruments to the holder of the instrument. The proceeds of the issue are recorded directly in equity, and held at historical cost. Incremental costs directly attributable to the issue of equity instruments are shown in equity as a deduction from the proceeds, net of tax. Dividends and other returns to equity holders are recognised as a deduction from distributable reserves within equity when paid or declared by the Company.

Issued financial instruments or their components are classified as liabilities if the underlying contract results in a present obligation for the Company to either deliver cash, another financial asset, or a variable number of the Company's own equity shares to the holder of the instrument. Financial liabilities are measured at amortised cost, except for trading liabilities and liabilities designated at fair value, which are held at fair value through profit and loss.

Where issued financial instruments contain both liability and equity components, these are accounted for separately. The fair value of the debt is estimated first and the remainder of the proceeds are included within equity.

1 Accounting policies (continued)

Identification and measurement of impairment

At each balance sheet date the Company assesses whether there is objective evidence that financial assets not carried at fair value through the income statement are impaired. Financial assets are impaired when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset, and that the loss event has an impact on the expected future cash flows of the asset that can be estimated reliably. Examples of such events would include significant credit deterioration of the issuer such as a significant credit rating downgrade; default, delinquency or bankruptcy of the issuer; or another specific event which would lead to a decrease in expected future cash flows.

Impairment losses on assets carried at amortised cost are measured as the difference between the carrying amount of the financial assets and the present value of estimated future cash flows, discounted at the assets' original effective interest rate. Losses are recognised in the income statement and reflected in an allowance against the carrying value of the assets. Interest on the impaired asset continues to be recognised through the unwinding of the discount.

When a subsequent event, for example, reversal of one of the conditions outlined above, causes the amount of impairment loss to decrease, the impairment loss is reversed through the income statement.

Impairment losses on AFS investment securities are recognised by transferring the difference between the amortised acquisition cost and current fair value out of equity to the income statement. When a subsequent event causes the amount of impairment loss on an AFS debt security to decrease, the decrease in impairment loss is reversed through the income statement. Impairment losses on AFS equity securities are not reversed through the income statement.

Derivatives

Where contracts meet the definition of a derivative within IAS 39, they are recognised initially, and are subsequently remeasured, at fair value. All changes in fair value, except for certain gains and losses related to cash flow hedges, are recognised in the income statement within trading income as they arise. Fair values are obtained from quoted market prices in active markets, or using valuation techniques where an active market does not exist. Valuation techniques include discounted cash flow models, recent market transactions and option pricing models as appropriate. All derivatives are classified as assets when their fair value is positive or as liabilities when their fair value is negative. Derivatives are recognised using trade date accounting.

The company makes use of the exemption from derivative accounting permitted within the standard for regular way purchases and sales of securities – these are accounted for using trade date accounting - see above.

Financial assets and liabilities are offset and the net amount reported on the balance sheet if, and only if, the entity currently has a legally enforceable right of offset and there is an intention to settle on a net basis, or to realise an asset and settle the liability simultaneously. In many cases, even though master netting agreements are in place, the related assets and liabilities are presented gross on the balance sheet as these requirements are not met.

The value of derivative contracts has been adjusted to include the impact of counterparty credit risk ("CVA") and the cost and benefit of future funding ("FVA"). The impact of changes in the Company's own credit risk ("DVA") is materially included within the application of FVA. The Company is the beneficiary of an intercompany guarantee from BTMU which provides the Company with protection over a portfolio of corporate derivatives. This guarantee does not meet the definition in IAS 39 of a financial guarantee, and as such is accounted for as a credit derivative.

Collateral

Cash collateral pledged by the Company on derivative and other liabilities is classified as an asset within financial assets at amortised cost. Cash collateral pledged by counterparties is classified within financial liabilities at amortised cost. These balances are initially measured at fair value and subsequently measured at amortised cost.

Where securities are posted to counterparties as collateral against liabilities of the Company the security will be retained on the Company's balance sheet and will not impact the recorded liability. Collateral received in the form of securities is not recorded on the balance sheet.

Embedded derivatives

Derivatives may be embedded in other contractual arrangements. Embedded derivatives are treated as separate derivatives when their economic characteristics and risks are not clearly and closely related to those of the host; the terms of the embedded derivatives would meet the definition of a stand-alone derivative if they were contained in a separate contract; and the combined contract is not held for trading or designated at fair value. These embedded derivatives are measured at fair value with changes in fair value recognised in the income statement.

The Company has embedded derivatives within its issued structured notes portfolio, those notes are carried at fair value through profit and loss under the fair value option.

Equity finance assets

Equity finance assets are recognised initially, and are subsequently remeasured, at fair value. All changes in fair value, are recognised in the income statement within trading income as they arise. Fair values are obtained from quoted market prices in active markets, or using valuation techniques where an active market does not exist. Equity financing assets are recognised using trade date accounting.

1 Accounting policies (continued)

Hedge accounting

At the inception of a hedging relationship, the Company documents the relationship between the hedging instruments and the hedged items, its risk management objective and its strategy for undertaking the hedge. The Company also requires a documented assessment, both at hedge inception and on an ongoing basis (both prospective and retrospective effectiveness), of whether or not the hedging instruments are highly effective in offsetting the changes in the fair values of the hedged items attributable to the hedged risks. Hedges are designated by the Company as either: hedges of the change in fair value of recognised assets or liabilities ('fair value hedges') or hedges of the variability of cash flows attributable to a recognised asset or liability or a forecast transaction ('cash flow hedges').

Fair value hedges

Changes in the fair value of derivatives that are designated, and qualify, as fair value hedging instruments are recorded in the income statement, along with changes in the fair value of the hedged assets, liabilities or groups thereof that are attributable to the hedged risk. If a hedging relationship no longer meets the criteria for hedge accounting, the cumulative adjustment to the carrying amount of the hedged item is amortised to the income statement based on a recalculated effective interest rate over the residual period to maturity, unless the hedged item has been derecognised, in which case, it is released to the income statement immediately.

Cash flow hedges

The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised in shareholder's equity within the cash flow hedging reserve. Any gain or loss in fair value relating to an ineffective portion is recognised immediately in the income statement. Amounts accumulated in equity are recycled to the income statement in the periods in which the hedged item will affect profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity until the hedged transaction is recognised in the income statement. When a hedged forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the income statement.

Derecognition of financial assets and liabilities

Financial assets are derecognised when the rights to receive cash flows from the assets have expired; or when the Company has transferred both its contractual right to receive the cash flows of the financial assets, and substantially all the risks and rewards of ownership; or where control is not retained. Financial liabilities are derecognised when they are extinguished, that is when the obligation is discharged, cancelled or expired.

Fair value measurement of financial assets and liabilities

Fair value is the amount for which an asset could be sold, or a liability transferred, between knowledgeable, willing parties in an arm's length transaction on the measurement date.

When available, the Company measures the fair value of an instrument using quoted prices in an active market for that instrument. A market is regarded as active if quoted prices are readily and regularly available and represent actual and regularly occurring market transactions on an arm's length basis.

If the market for a financial instrument is not active, the Company establishes fair value using valuation techniques. Valuation techniques include using recent arm's length transactions between knowledgeable, willing parties (if available), reference to the current fair value of other instruments that are substantially the same, discounted cash flow analysis and option pricing models. The chosen valuation technique makes maximum use of market inputs, relies as little as possible on estimates specific to the Company, incorporates all factors that market participants would consider in setting a price, and is consistent with accepted economic methodologies for pricing financial instruments. Inputs to valuation techniques reasonably represent market expectations and measures of the risk-return factors inherent in the financial instrument. The Company calibrates valuation techniques and tests them for validity using prices from observable current market transactions in the same instrument or based on other available observable market data.

When unobservable market data has a significant impact on the valuation of financial instruments and the model valuations indicate initial profits or losses on the transaction, the entire initial gain or loss is not recognised immediately in the income statement. The initial gain or loss is measured as the difference in fair value indicated by the valuation model price and the transaction price. These gains or losses are deferred and recognised over the life of the transaction on a systematic basis, or when the inputs become observable, or the transaction matures or is closed out, or when the Company enters into an eligible offsetting or economic hedging transaction which provides a market data point to demonstrate observability of the unobservable input(s). Refer to Note 23 for further detail on the fair value of financial instruments.

1 Accounting policies (continued)

Transactions in which the Company acts as an agent

Where the Company acts as an intermediary on behalf of another entity and does not have exposure to the significant risks and rewards associated with the activities performed, it is determined to be acting in an agency capacity. When examining relationships, MUS(EMEA) reviews which entity has primary responsibility for providing services to customers, has inventory risk, has latitude to establish prices, or bears credit risk of the transaction. In the absence of evidence or analysis to the contrary, MUS(EMEA) will follow the legal form of transactions and arrangements will be reported as principal relationships.

When the Company acts as an agent on behalf of another entity, neither the amounts collected from clients on behalf of the principal entity nor the amounts paid away to the principal entity are recorded in revenue. Rather, MUS(EMEA) records revenues as the commissions received from the principal, such revenue is accrued as the service is provided. Similarly, unsettled amounts relating to agency trading will not be shown on the balance sheet.

During the period, certain contracts relating to the Equity Sales business were reviewed and it was determined that the Company is acting in an agency capacity on behalf of an affiliate. The accounting treatment for transactions within this business was changed accordingly. The impact of applying this change in accounting policies to the current and comparative period was £ Nil.

Management fees and commission

Management fees and commission are recognised in the period during which the management service has been provided.

Client money segregation

The Company holds money on behalf of some clients in accordance with the Client Money Rules of the Financial Conduct Authority. Such monies and the corresponding amounts due to clients are not held on the balance sheet as the clients retain beneficial ownership.

Net interest income

The interest balances presented within the income statement represent the returns and costs to the firm of holding regulatory buffer assets and long term investment positions. These positions are held and managed within the Treasury function. Interest income represents coupon income and amortisation of any premium or discount arising upon purchase of AFS investments and certain reverse repurchase agreements treated as loans and receivables. Interest expense represents the cost of funding these positions and includes the cost of repurchase agreements held as liabilities at amortised cost, interest payable on subordinated debt, and interest costs on other sources of funds that support these investments.

Any coupon receivable or payable on items which are part of the trading activities of the Company are included directly within Trading Income.

Foreign currencies

The financial statements are presented in pounds sterling which is the presentation and functional currency of the Company.

Monetary assets and liabilities denominated in foreign currencies and open forward foreign exchange contracts are translated using the rate of exchange prevailing at the balance sheet date. Gains or losses on translation are included in the income statement.

The assets and liabilities of the Company recognised in foreign currencies are translated to the Company's functional currency at the exchange rates of the reporting date. The income and expenses of the Company are translated to the Company's functional currency at the exchange rates at the dates of the transactions.

Property, plant and equipment and intangible assets

Property, plant and equipment and intangible assets are measured at cost less accumulated depreciation and any accumulated impairment losses.

Expenditure to bring purchased software into operational use and internally developed software are recognised as intangible assets when the Company considers that the software will be used in a manner that will generate future economic benefits and can reliably measure the costs of development.

All fixed assets are reviewed for impairment on an annual basis. Assets are impaired where it is considered that the future economic benefit of the asset is lower than its carrying amount. Such impairment losses are included directly in the income statement.

Depreciation is provided to write off the cost less estimated residual value of tangible fixed assets and intangible software assets by equal instalments over their estimated useful lives as follows:

Leasehold improvements	10 – 25 years or over the remaining term of the lease
Office furniture and fittings	5 years
Office machinery and equipment	3 – 5 years
Intangible software	3 – 7 years
Finance lease assets	Lease term

1 Accounting policies (continued)

Leases

A lease is classified at the date that the Company enters the agreement as either a finance lease or an operating lease. A lease that transfers substantially all the risks and rewards incidental to ownership to the Company is classified as a finance lease.

Finance leases are capitalised as assets at the lower of the fair value of the property which is being leased or the present value of the minimum lease payments. The income statement is affected by both depreciation of the capitalised asset and interest on the minimum lease payment liability.

An operating lease is a lease other than a finance lease. Operating lease payments are recognised as an expense on a straight line basis over the lease term.

Taxation

Taxation comprises current and deferred tax. Current tax and deferred tax are recognised in the income statement except to the extent that they relate to items recognised directly in equity.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognised in respect of all temporary differences and tax losses that have originated but not reversed by the balance sheet date. Temporary differences are divergences between the Company's results for tax purposes and its results as stated in the financial statements that arise from the inclusion of income and expenses in tax assessments in periods different from those in which they are recognised in the financial statements. Temporary differences and tax losses are taken into account if they have originated prior to the balance sheet date and are expected to reverse in one or more future periods.

Deferred tax is calculated at the tax rates that are expected to be applied to temporary differences or tax losses when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities against current tax assets, and they relate to taxes levied by the same tax authority on the same taxable entity, or on different taxable entities which intend to settle current tax liabilities and assets on a net basis.

A deferred tax asset is recognised for unused tax losses and other deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax balances are not discounted.

Employee benefits

Staff are remunerated through both salary and annual performance based discretionary compensation awards. Performance based awards are calculated annually, and reflect the performance of both the individual and the Company during that annual period. Portions of performance based awards are paid by the Company on deferred terms. From 2011 onwards, a portion of these deferred awards for certain employees subject to the PRA's Remuneration Code is linked to the performance of the share price of MUFG. These awards are termed Notional Stock Units (NSU's).

Where payments are made on a deferred basis and the cash value is fixed at the award date, the Company recognises the costs of the deferred awards during the period that the award is made, even though cash payments will not be made until future periods. The Company considers that this treatment most effectively represents the costs of employee compensation for the period.

Where payments are made on a deferred basis and the cash value is linked to the MUFG share price, the Company amortises the expected cost of the award across the entire deferral period, and records as an expense only that portion which is deemed to have accrued during the current period.

1 Accounting policies (continued)

Pensions

The Company maintains both a defined contribution pension scheme and a defined benefit pension scheme (the defined benefit scheme is closed to new entrants and to future accruals).

For the defined contribution scheme, pension costs are charged to the income statement which represent the contributions payable to the scheme in respect of the accounting period.

For the defined benefit scheme, pension scheme assets are measured using market value. Pension scheme liabilities are measured using a projected unit method and discounted at the current rate of return on high quality corporate bonds of equivalent term and currency to the liability. Any increase in the present value of the liabilities of the Company's defined benefit pension scheme expected to arise from employee service in the period is charged to Profit on ordinary activities before taxation. The expected return on the scheme's assets and the increase during the period in the present value of the scheme's liabilities arising from the passage of time are included in administrative expenses. Actuarial gains and losses are recognised in the statement of total comprehensive income. Deficits in the scheme are recognised in the Company's balance sheet. Surpluses are only recognised to the extent that they are recoverable through reduced contributions in the future or through refunds from the schemes.

The Company recognises the effect of material changes to the terms of its defined benefit pension scheme which reduce future benefits as curtailments; gains and losses are recognised in the income statement when the curtailments occur.

The Company revalues its defined benefit scheme at 30 June and 31 December each year, in consultation with the scheme's actuaries. The assumptions underlying the calculations are used to determine the expected income statement charge for the year going forward.

Adoption of new and revised Standards

In the current year, the following new and revised Standards and Interpretations have been adopted when preparing the amounts reported in these Financial Statements. Only those Standards which are pertinent to the Company are summarised:

- Amendments to IAS 12: Recognition of Deferred Tax Assets for Unrealised Losses

Amendments made to IAS 12 in January 2016 clarify the accounting for deferred tax where an asset is measured at fair value and that fair value is below the asset's tax base. The amendments confirm items relating to: the existence of temporary differences when the carrying amount of an asset is less than its tax base; assumptions of recovery values higher than carrying values in estimation of future taxable profits are acceptable; recoverability of deferred tax assets must be assessed in combination with other deferred tax assets of a similar type where tax law restricts the sources of taxable profits against which they can be recovered; and tax deductions resulting from the reversal of deferred tax assets are excluded from estimated future taxable profits used to evaluate the recoverability of those assets. These amendments do not have any impact on the Company's financial statements in the current or prior period.

- Amendments to IAS 7: Disclosure Initiative

Amendments made to IAS 7 require additional disclosure to explain changes in liabilities arising from financing activities. This includes changes arising from cash flows and non-cash changes such as acquisitions, disposals, accretion of interest and unrealised exchange differences. Changes in financial assets must be included in this disclosure if the cash flows are included in cash flows from financing activities.

- Annual improvements 2014-2016 cycle: Amendments to IFRS 12

The amendments clarify that the disclosure requirements of IFRS 12 apply to interests in entities that are classified as held for sale, except for the summarised financial information. These amendments do not have any impact on the Company's financial statements in the current or prior period.

1 Accounting policies (continued)

Future Accounting Developments

The following standards, which have been issued but are not yet required to be applied, are likely to have an impact on the entity's financial reports (note, amendments which are not expected to have an impact on the Company's financial reporting have not been summarised here):

IFRS 9 Financial Instruments
IFRS 9, which will replace IAS 39 Financial Instruments: Recognition and Measurement, is effective for periods beginning on or after 1 January 2018 and was endorsed by the EU in November 2016. The standard is separated into three component parts, the expected impact of each is detailed below:

Classification and measurement
IFRS introduces new requirements for the categorisation of financial assets which will be based on the business model under which those assets are managed and their contractual cash flow characteristics. Financial assets will be measured either at:

- amortised cost, where the business model is to originate or buy and hold the asset in order to collect contractual cash flows, and those cash flows represent only repayments of principal and interest,
- fair value through profit and loss, where the business model is short term profit taking (trading book) or fair value option elections are made, or
- fair value through Other Comprehensive Income, where assets are held in a business model whose objective is achieved either by sale or collection of contractual cash flows; and the contractual cash flows represent only repayments of principal and interest.

The Company may elect to carry assets at fair value where doing so significantly reduces measurement or recognition inconsistencies (i.e. where measuring assets and liabilities on different bases would create an accounting mismatch).

Consistent with the current treatment under IAS 39, the vast majority of Company's assets will be recognised at fair value through profit and loss within the trading book under IFRS 9 reflecting the business model of client service and short term holdings. Positions are typically maintained to service client requests, are traded directly or risk exposures of those positions are traded through mitigating transactions to protect profits. Certain businesses hold assets for longer periods in order to provide funding to clients, these exposures typically contain exotic risks (e.g. equity or structured credit) and would not meet the solely payments of principal or interest requirements of the standard. As such, these are assets will also be carried at fair value through profit and loss.

Certain positions within the Company's Treasury business do not meet these criteria. The Company's liquidity buffer asset portfolio consists of liquid high credit quality debt securities which are held to satisfy regulatory requirements; asset sales from this portfolio may be required to support cash needs of the business. The liquidity buffer is predominantly held in the form of securities rather than cash in order to enhance yield. As such, this portfolio will be carried at fair value through other comprehensive income. The Treasury business also source liquid assets through securities borrowing transactions which are typically held to term and which are comprised of contractual cash flows representing only principal and interest – these trades will be carried at amotised cost.

The accounting for financial liabilities is largely unchanged, and the Company expects to continue with the current classification of these positions. IFRS 9 requires entities to record changes in the fair value of liabilities for which the fair value option has been elected due to movements in the credit risk of the entity through Other Comprehensive Income. The Company maintains a portfolio of issued structured notes and intercompany loans under the fair value option (see Note 17). These liabilities are not actively traded in the market, with notes typically issued via private placement to Japanese investors via an affiliate. The valuation of these positions currently includes consideration of the Company's cost of funds, which includes the impact of own credit risk. The Company continues to assess practical methods for separating movements in value of these liabilities due to changes in its own credit risk from other fair value movements in the absence of quoted CDS or direct debt issuance to the market which would allow such spreads to be inferred. In light of the observed stability of the proxy spread for own credit, the Company does not expect this change to have a material impact.

Impairment
Under IFRS 9, expected credit losses are required to be recognised for all assets which are not carried at fair value through profit and loss. 12 months expected losses must now be recognised directly in the Income Statement upon initial recognition of assets, which increases to lifetime expected losses where assets are subject to significant credit deterioration after initial recognition.

The Company will include expected credit losses against portfolios which are not carried at fair value through profit and loss as noted above. Due to the high credit quality of the securities held within this portfolio and the collateralisation available for securities borrowing transactions, the estimated size of expected credit losses at transition is calculated in a conservative manner to reflect externa credit ratings, implied probability of default, and market assumed recovery in the event of default. The most conservative estimate from this process is a loss provision of approximately £250k against a portfolio size of £1,500 million. Due to the retrospective application of IFRS 9, this transition adjustment will affect retained earnings. The key driver of volatility in this balance in the future is likely to be portfolio size.

Hedge accounting
New rules are provided for hedge accounting, more closely aligned with risk management practices, reducing the necessity for quantitative effectiveness testing, and removing rules for voluntary designation and de-designation outside of documented risk management activity. IFRS 9 includes an option for reporting entities to defer adoption of the hedge accounting guidance and to retain the hedge accounting guidance within IAS 39. The Company intends to make this accounting policy choice, and will continue to use the IAS 39 model. This accounting policy choice will be reviewed in future periods to determine the benefits of transitioning to the new IFRS 9 model. It is expected that this policy choice will be removed when the standard governing macro hedge accounting is issued.

1 Accounting policies (continued)

IFRS 15 Revenues on contracts with customers

IFRS 15 is effective for periods beginning on or after 1 January 2018 and was endorsed by the EU in September 2016. It will replace IAS 18 Revenue and IAS 11 Construction Contracts, and applies to all contracts with customers except leases, financial instruments and insurance contracts. It establishes a stepwise model for revenue recognition which requires identification of contracts, separating those contracts into discrete performance obligations, allocating consideration to each obligation, and recognising revenue only once each obligation is satisfied.

Due to the nature of the Company's business as a client service focussed financial institution, much of the Company's revenue arises from financial instrument transactions and is not within the scope of this standard. As such, the implementation analysis has focussed on business areas where services are provided to clients or affiliates, particularly within the Capital Markets and Structured businesses. Due to the short term nature of many of the Company's contracts and the limited nature of services specified within those contracts, the adoption of IFRS 15 is not expected to have a material impact on the timing of revenues recognised by the Company.

IFRS 16 Leases

IFRS 16 requires lessees to record operating leases on the Balance Sheet as an asset (the right to use the leased item) and a financial liability (the discounted value of future lease payments). An optional exemption exists for short-term and low-value leases. The income statement is affected by these changes, and the operating lease expenses are replaced by depreciation of the right of use asset and interest accretion representing the reversal of discounting against future lease payments. Operating lease payments are currently included within Operating cash flows under current accounting standards, under IFRS 16, cash payments against operating leases will be reflected as financing cash flows within the Company's cash flow statement, with any interest on the lease liability recorded as operating cash flows.

The Company estimates that assets and liabilities will increase by approximately £50.0 million on adoption of this standard, principally comprised of right of use assets and obligations to make future lease payments against the premises occupied by the Company (leased until 2029). After adoption, corresponding cash out flows of approximately £4.2 million will be reported as Financing cash flows rather than Operating cash flows.

2 Interest income and similar income

	2017 £'000	2016 £'000
Interest on non-trading assets	18,325	31,142
Interest on loans and receivables from banks	2,601	(1,387)
	20,926	**29,755**

'Interest on loans and receivables from banks' includes reverse repos reported at amortised cost, which were impacted by negative EUR and JPY rates during 2016 and 2017.

3 Interest expense

	2017 £'000	2016 £'000
Interest on non-trading liabilities	1,460	4,680
Interest on loans and payables to banks	595	890
Interest on subordinated liabilities	2,378	7,199
	4,433	**12,769**

'Interest on subordinated liabilities' refers to intercompany subordinated debt issued to the Company's immediate parent, MUSHD (refer Note 19), impacted by the partial repayment of Tier 2 loans totalling JPY119.175 billion in December 2016.

4 Administrative expenses

	2017 £'000	2016 £'000
Wages and salaries	121,019	106,808
Retirement benefits	5,645	4,636
Social security costs	17,014	14,675
Personnel expenses	**143,678**	**126,119**
Auditor's remuneration (Note 5)	699	868
Operating lease rentals: property	3,521	844
Other administrative expense	50,976	64,305
General and administrative expenses	**55,196**	**66,017**
Total administrative expenses	**198,874**	**192,136**

The average number of employees of the Company was 629 (2016: 587), split 164:465 (2016: 151:436) between front office and support staff respectively.

'Other administrative expense' included a charge of £8.925m in December 2016 related to a settlement agreement reached with the PRA. Refer to the 2016 Financial Statements for details.

'Total administrative expenses' includes research and development expenditure of £5.6m (2016: £6.3m) representing employee wages and salaries, project contractor, consumable and software costs.

5 Auditor's remuneration

The analysis of the auditor's remuneration is as follows:

	2017 £'000	2016 £'000
Fees payable to the Company's auditor for audit and other services:		
Statutory audit fees	465	415
Audit related assurance services	61	85
Other taxation advisory services	-	20
Other services	-	170
Other assurance services	121	128
Services relating to corporate finance	34	32
	681	850
Fees payable to the Company's auditor in respect of associated pension schemes:	18	18
Total auditor's remuneration	**699**	**868**

6 Share based payment plans

Notional Stock Units

The Company awarded NSUs to a number of employees during the year. The NSUs are deferred over a period of 3, 5 or 7 years, depending on award date and the individuals role, and track the performance of MUFG shares (see accounting policies).

	2017		2016	
	No. Units ('000)	**Value (£'000)**	**No. Units ('000)**	**Value (£'000)**
No. of NSUs outstanding as at 1 January	**4,740**		**4,445**	
Granted during the year:				
No. of NSUs granted	1,995		1,969	
Value in GBP '000 equivalent at grant date		10,276		10,332
Less:				
No. of NSUs vested during the year	(2,265)		(1,674)	
Average share price at vesting / payment (JPY)		691		524
No. of NSUs forfeited / cancelled (unvested)	-		-	
No. of NSUs as at 31 December	**4,470**		**4,740**	
Fair value of outstanding NSUs at 31 December		**22,810**		**21,919**

7 Retirement benefits

The Company provides a defined contribution pension scheme, the Group Personal Pension Plan ("GPPP"), for employees of the Company. The assets of the scheme are held separately from those of the Company in an independently administered fund. The cost for the period recognised in the income statement was £5.6 million (2016: £4.6 million).

The Company also provides a funded, final salary, defined benefit pension scheme which was closed to new entrants and future accrual in 2011. The assets of the scheme are held separately from those of the Company in a segregated fund administered by trustees. The scheme is deemed to be a registered pension scheme under the terms of Schedule 36 of the Finance Act 2004 with scheme funding target objectives set by this act. Pension valuations are undertaken by independent qualified actuary with reporting guidelines set by the Technical Actuarial Standard with calculations consistent with the International Accounting Standard ("IAS19").

7 Retirement benefits (continued)

An update to the latest actuarial valuation was performed as at 31 December 2017 and the principal actuarial assumptions at the balance sheet date were as follows:

	2017 %	2016 %
Discount rate	2.60	2.90
RPI inflation assumption	3.45	3.50
CPI inflation assumption	2.45	2.50
LPI pension increase assumption	3.45	3.50

The discount rate assumption is based upon published corporate bond indices. The inflation assumptions reference Bank of England published yield curve data.

The underlying mortality assumption is based upon the standard table known as S2PXA_L on a year of birth usage with CMI_2016 future improvement factors with a long term annual rate of future improvement of 1.25% p.a. (2016: S2PXA_L on a year of birth usage with CMI_2015 future improvement factors with a long term annual rate of future improvement of 1.25% p.a.). This results in the following life expectancies:

- Male age 65 now has a life expectancy of 23 years (previously 23 years)
- Female age 65 now has a life expectancy of 24 years (previously 24 years)

The amounts recognised in the balance sheet as at the year end are as follows:

	2017 £'000	2016 £'000
Present value of funded obligations	(185,795)	(189,491)
Fair value of plan assets	201,644	181,780
Recognisable surplus / (deficit) in the scheme	**15,849**	**(7,711)**
Related deferred tax asset / (liability)	(4,200)	2,083
Net pension asset / (liability)	**11,649**	**(5,628)**

The amounts recognised in the income statement within administrative expenses total £114k debit (2016: £527k credit). The projected income for the calendar year 2018 is £516k credit within administrative expenses.

All scheme costs are met directly by the Company and are therefore excluded from these disclosures.

Changes to the present value of the scheme liabilities for the year end are as follows:

	2017 £'000	2016 £'000
Present value of unfunded obligation at opening	189,491	144,950
Interest cost	5,478	5,775
Actuarial remeasurement	3,592	41,718
Benefits paid	(12,766)	(2,952)
Present value of obligation at closing	**185,795**	**189,491**

Changes in the fair value of the scheme assets for the year end are as follows:

	2017 £'000	2016 £'000
Fair value of plan assets at opening	181,780	154,450
Expected return on plan assets	5,364	6,302
Actuarial remeasurement	19,639	16,646
Benefits paid by fund	(12,766)	(2,952)
Contributions paid by the Company	7,627	7,334
Fair value of scheme assets at closing	**201,644**	**181,780**

The expected contribution to be paid by the Company for the forthcoming year (year ending 31st December 2018) is £6.6 million.

7 Retirement benefits (continued)

The market value of total scheme assets for the year end are as follows:

	2017 £'000	2016 £'000
UK equities	46,165	42,646
Overseas equities	121,351	105,883
Absolute return	29,926	32,408
Property	1,990	-
Cash	2,212	843
Total	**201,644**	**181,780**

All scheme assets have a quoted market price in an active market. The assets of the scheme are held separately from those of the Company in funds under the control of the Trustees of the scheme.

The amounts recognised in Other Comprehensive Income for the year end are as follows:

	2017 £'000	2016 £'000
Actual return less expected return on scheme assets	19,639	16,646
Experienced gains and losses arising on scheme liabilities	3,395	2,956
Changes in assumptions underlying the present value of scheme liabilities	(6,987)	(44,674)
Actuarial gain / (loss) recognised in OCI	**16,047**	**(25,072)**

Movement in recognisable surplus / (deficit) during the year are as follows:

	2017 £'000	2016 £'000
(Deficit) / surplus at start of year	(7,711)	9,500
(Expense) / income recognised in income statement	(114)	527
Contributions paid by the company	7,627	7,334
Recognised actuarial gain / (losses)	16,047	(25,072)
Surplus / (deficit) at end of year	**15,849**	**(7,711)**

Analysis of present value of scheme liabilities:

	2017 %	2016 %
Deferred members	77	78
Current pensioners	23	22
Total	**100**	**100**

The below table shows the impact on the present value placed on the scheme's liabilities of the stated changes to the actuarial assumptions (refer page 34). These sensitivities have been determined by a full recalculation of the present value using the different assumptions and are therefore fully accurate (2016: same approach).

	2017 %	2016 %
Discount rate +/- 0.5%	-11 / +13	-11 / +13
RPI and CPI +/- 0.5%	+4 / -3	+4 / -4
Life expectancy +/- 1 year	+4 / -4	+3 / -3
Pension increase (in payment and deferment) +/- 0.5%	+4 / -3	n/a

The weighted average duration of the scheme liabilities is approximately 25 years (2016: 25 years).

8 Applicable taxes

	2017 £'000	2016 £'000
UK corporation tax		
Current year	(20,767)	(15,731)
Adjustments in respect of prior years	2,352	-
	(18,415)	(15,731)
Foreign tax		
Current year	(1,348)	(1,026)
Adjustments in respect of prior years	-	-
Total current tax	**(19,763)**	**(16,757)**
Deferred tax		
Origination and reversal of timing differences	(6,910)	(7,686)
Effect of reduction in rate used to recognise deferred tax assets	(339)	(464)
Adjustments in respect of prior years	(1,264)	6,056
Total deferred tax	**(8,513)**	**(2,094)**
Total tax expense	**(28,276)**	**(18,851)**

Corporation tax is calculated at 27.25% (2016: 28%) of the estimated taxable profit for the year The decrease in tax rate reflects a reduction in the standard rate of corporation tax from 20% to 19% effective 1 April 2017. The Company continues to be subject to the 8% corporation tax surcharge applicable to banks and brokers.

The charge for the year can be reconciled to the profit in the income statement as follows:

	2017 £'000	2016 £'000
Profit on ordinary activities before taxation	108,099	78,750
Tax at the UK corporation tax rate of 27.25% (2016: 28%)	(29,457)	(22,050)
Tax effect of expenses that are not deductible in determining taxable profits	(402)	(3,415)
Foreign tax suffered	(982)	(739)
Deferred tax prior year adjustment	(1,264)	6,056
Effect of reduction in rate used to recognise deferred tax assets	(339)	(464)
Realisation of deferred tax assets previously valued below current year statutory rate	216	381
Current tax prior year adjustment	2,352	-
Share of group bank surcharge allowance	1,600	1,380
Tax expense for the year	**(28,276)**	**(18,851)**

In addition to the amount charged to the income statement, the following amounts related to tax have been recognised in Other comprehensive income:

	2017 £'000	2016 £'000
Current tax	1,402	-
Deferred tax		
Items that will not be reclassified subsequently to profit and loss		
Remeasurement of net defined benefit liability	(4,253)	6,104
Items that may be reclassified subsequently to profit or loss		
Available for sale financial assets losses / (gains) in period	17	(1,408)
Cash flow hedges (gains) in period	(87)	(171)
Total income tax recognised in other comprehensive income	**(2,921)**	**4,525**

8 Applicable taxes (continued)

Deferred tax assets

The following are the deferred tax assets and liabilities recognised by the Company and movements thereon during the current and prior reporting period.

	Balance as at 1 January 2017 £'000	Charge to profit or loss £'000	Charge to OCI £'000	Transferred from other receivables £'000	Balance as at 31 December 2017 £'000
Accelerated tax depreciation	5,952	(1,228)	-	-	4,724
Unused tax credits	802	-	-	(802)	-
Deferred compensation	10,382	(858)	-	-	9,523
Spreading of IFRS 13 transitional adjustment	2,311	(365)	-	-	1,944
Cash flow hedge reserve	(116)	-	(87)	-	(203)
Available for sale financial assets	(1,147)	217	17	-	(914)
Retirement benefit obligations	2,083	(2,029)	(4,253)	-	(4,200)
Tax losses	11,773	(4,250)	-	-	7,522
Total Balance	**32,040**	**(8,513)**	**(4,323)**	**(802)**	**18,396**

Deferred tax assets are valued at the applicable corporation tax rate based on the period in which the underlying temporary difference is expected to reverse. The deferred tax assets above have been recognised based on supporting profit forecasts demonstrating sufficient future profits against which the assets can be utilised. Under UK tax rules, tax losses can be carried forward indefinitely. The offset of pre April 2015 losses carried forward by UK banks and brokers is limited to 25% of taxable profits. Whilst the restriction on the use of carried forward losses will result in them being utilised over a longer period it should not impact the ultimate recoverability of the losses and hence a deferred tax asset has been recognised.

9 Notes to the Cash flow statement

Cash and cash equivalents comprise cash and short-term bank deposits with an original maturity of three months or less, net of outstanding bank overdrafts. The carrying amount of these assets is approximately equal to their face value. Cash and cash equivalents as shown in the statement of cash flows can be reconciled to the related items in the balance sheet position as shown below.

	2017 £'000	2016 £'000
Cash and balances at central banks	976,430	975,454
Deposits by banks repayable on demand	(88,311)	(72,392)
Total cash and cash equivalents	**888,119**	**903,062**

The table below details changes to the Company's liabilities arising from financing acitivities, including both cash and non cash changes.

	Balance as at 1 January 2017 £'000	Financing cash flows £'000	Changes in fair values £'000	Effect of changes in foreign exchange rates £'000	Balance as at 31 December 2017 £'000
Own issued notes	2,098,543	(418,862)	105,521	(127,339)	1,657,863
Commercial paper	476,070	826,797	(786)	(1,478)	1,300,603
Other financial liabilities	865,220	200,432	(6,777)	(66,799)	992,076
MUSHD loan facility	1,123,704	(269,973)	(246)	(139,014)	714,471
Subordinated liabilities	309,151	-	(7)	(19,106)	290,038
Total liabilities from financing activities	**4,872,688**	**338,394**	**97,705**	**(353,736)**	**4,955,051**

10 Trading portfolio financial assets

	2017 £'000	2016 £'000
Government bonds	3,092,975	2,850,854
Corporation bonds	954,644	780,463
Other public sector securities	104,057	144,421
Total debt securities	**4,151,676**	**3,775,738**
Equity instruments	4,306,984	1,583,271
Total trading portfolio financial assets	**8,458,660**	**5,359,009**
Of which listed:		
Debt securities	3,682,197	3,544,184
Equity instruments	2,363,457	336,525
Of which unlisted:		
Debt securities	469,479	231,554
Equity instruments	1,943,527	1,246,746
	8,458,660	**5,359,009**

11 Derivative financial instruments

	2017		
	Notional amount £'000	Fair value assets £'000	Fair value liabilities £'000
Derivatives held for trading			
Foreign exchange contracts	236,951,624	4,406,534	3,675,016
Interest rate contracts	2,383,234,225	8,148,835	7,407,319
Credit derivative contracts	24,312,496	538,001	279,104
Equity contracts	18,594,994	159,280	205,052
Commodities contracts	808,260	189,350	189,822
Total trading contracts	**2,663,901,599**	**13,442,000**	**11,756,313**
Derivatives designated as fair value hedges			
Interest rate swaps contracts	488,573	-	68
Derivatives designated as cash flow hedges			
Forward foreign exchange contracts	401,532	3,575	7,015
Total hedging contracts	**890,105**	**3,575**	**7,083**
Total derivatives financial instruments	**2,664,791,704**	**13,445,575**	**11,763,396**

	2016		
	Notional amount £'000	Fair value assets £'000	Fair value liabilities £'000
Derivatives held for trading			
Foreign exchange contracts	214,337,351	7,726,997	7,763,330
Interest rate contracts	2,862,926,525	10,528,480	10,062,046
Credit derivative contracts	21,085,090	794,971	168,581
Equity contracts	8,878,602	123,653	246,618
Commodities contracts	891,498	110,042	110,099
Total trading contracts	**3,108,119,066**	**19,284,143**	**18,350,674**
Derivatives designated as fair value hedges			
Interest rate swaps contracts	841,691	4,389	18,923
Derivatives designated as cash flow hedges			
Forward foreign exchange contracts	361,568	8,448	27,579
Total hedging contracts	**1,203,259**	**12,837**	**46,502**
Total derivatives financial instruments	**3,109,322,325**	**19,296,980**	**18,397,176**

11 Derivative financial instruments (continued)

OTC credit derivatives include a credit derivative asset, which relates to a financial guarantee provided by a group company, BTMU, for the uncollateralised derivatives exposures within a portfolio of corporate counterparties. At year end the present value of this derivative totalled £249m (2016: £558m), this amount is offset by a CVA adjustment in respect of the exposure to the underlying corporate counterparties. This largely pertains to interest rate and foreign exchange contracts. The movement in these balances is driven by a narrowing of credit spreads during the period, portfolio amendments and a refinement of the model in line with evolving market practice (£nil net profit and loss impact).

CVA is measured on a portfolio basis by counterparty, and later allocated at a transaction level for financial reporting; allocations are based on absolute derivative notional values. The allocation methodology was refined during 2017 to include derivative transactions by counterparty across both asset and liability positions (both were already included in the portfolio calculation). Prior to this change, allocations were only made to derivatives in an asset position. This refinement is considered to better reflect the valuation of each underlying position that makes up the portfolio, as CVA can arise on both asset and liability positions. If this change were applied to the 2016 balances, the impact would increase derivative balance sheet assets and liabilities by £191m.

Gains and losses arising from fair value hedges:	2017 £'000	2016 £'000
On hedging instruments	11,642	2,480
On the hedged items attributable to the hedged risk	(10,473)	(2,167)
Net gains	**1,169**	**313**

The gains and losses on ineffective portions of fair value hedges are recognised immediately in Trading Income.

The net movement in cash flow hedging reserves comprises additions to the balance from movements in the value of derivatives designated in effective hedges and reclassifications of balances from the reserve into Trading Income. The closing reserve balance is presented net of tax. Reserve balances are transferred to the income statement in the same periods during which the hedged items affect profit or loss. The gains and losses on ineffective portions of derivatives designated in cash flow hedging relationships are recognised immediately in Trading Income in the Income statement. During the year, the ineffectiveness recorded in the Income statement was not significant (2016: not significant).

Fair value hedges principally consist of interest rate swaps that are used to protect against changes in the fair value of bonds due to movements in market interest rates.

Cash flow hedges consist of foreign currency exchange contracts to hedge the foreign currency risks arising from recognised financial assets denominated in foreign currencies.

12 Financial instruments available for sale

The following table gives the carrying value (fair value) of available for sale securities by major classifications.

	2017 £'000	2016 £'000
Government bonds	459,902	947,169
Other public sector securities	358,706	810,087
Total debt securities	**818,608**	**1,757,256**
Equity instruments	131	125
Total available for sale securities	**818,739**	**1,757,381**

Available for sale financial investments with unrealised losses of more than twelve months have been assessed for impairment. Based on the credit risk profile of the counterparties involved, it has been determined that impairment has not arisen at this time.

13 Intangible assets

	Software £'000	Capital lease asset £'000	Total £'000
Cost			
At 1 January 2016	108,482	499	108,981
Additions	16,959	-	16,959
Impairment	-	-	-
Disposals	(92)	-	(92)
At 31 December 2016	**125,349**	**499**	**125,848**
Additions	30,700	593	31,293
Impairment	(613)	-	(613)
Disposals	(181)	-	(181)
At 31 December 2017	**155,255**	**1,092**	**156,347**
Amortisation			
At 1 January 2016	62,843	38	62,881
Charge for the Year	12,711	104	12,815
Disposals	(20)	-	(20)
At 31 December 2016	**75,534**	**142**	**75,676**
Charge for the Year	14,645	269	14,914
Disposals	(36)	-	(36)
At 31 December 2017	**90,143**	**411**	**90,554**
Carrying amount:			
At 31 December 2016	**49,815**	**357**	**50,172**
At 31 December 2017	**65,112**	**681**	**65,793**

14 Property, plant and equipment

	Leasehold improve-ments £'000	Office furniture & fittings £'000	Office machinery & equipment £'000	Capital lease asset £'000	Total £'000
Cost					
At 1 January 2016	17,065	1,483	18,848	1,290	38,686
Additions	1,827	20	1,453	-	3,300
Disposals	(5,572)	(20)	(251)	-	(5,843)
At 31 December 2016	**13,320**	**1,483**	**20,050**	**1,290**	**36,143**
Additions	722	78	3,945	2,414	7,159
Disposals	(43)	-	(9)	-	(52)
At 31 December 2017	**13,999**	**1,561**	**23,986**	**3,704**	**43,250**
Depreciation					
At 1 January 2016	4,757	1,418	15,703	98	21,976
Charge for the year	830	17	1,449	268	2,564
Disposals	(1,507)	-	(187)	-	(1,694)
At 31 December 2016	**4,080**	**1,435**	**16,965**	**366**	**22,846**
Charge for the year	884	18	1,217	948	3,067
Disposals	(10)	-	(6)	-	(16)
At 31 December 2017	**4,954**	**1,453**	**18,176**	**1,314**	**25,897**
Carrying amount:					
At 31 December 2016	**9,240**	**48**	**3,085**	**924**	**13,297**
At 31 December 2017	**9,045**	**108**	**5,810**	**2,390**	**17,353**

15 Other assets

	2017 £'000	2016 £'000
Prepayments and accrued income	11,025	7,915
Current taxation	3,435	4,237
Pension asset (Note 7)	15,849	-
Other debtors - amortised cost	225,496	361,318
	255,805	**373,470**

'Other debtors – amortised cost' is driven by margin deposits at brokers and central clearers £168m (2016: £315m).

16 Trading portfolio financial liabilities

	2017 £'000	2016 £'000
Government bonds	3,883,649	4,488,389
Corporation bonds	93,815	157,744
Other public sector securities	15,153	8,336
Total debt securities	**3,992,617**	**4,654,469**
Equity instruments	1,775,230	892,233
Total trading portfolio financial liabilities	**5,767,847**	**5,546,702**
Of which listed:		
Debt securities	3,977,467	4,635,305
Equity instruments	1,707,292	892,233
Of which unlisted:		
Debt securities	15,150	19,164
Equity instruments	67,938	-
	5,767,847	**5,546,702**

17 Financial liabilities designated at fair value

	2017 £'000	2016 £'000
Own issued notes	1,657,863	2,098,543
Commercial paper	1,300,603	476,070
Other financial liabilities	992,076	865,220
MUSHD loan facility	714,471	1,123,704
	4,665,013	**4,563,537**

Own issued notes include issuances with structured payment profiles. The Company issues these notes to raise term funding and satisfy investor demand, and carries them at fair value through profit and loss. The structured return profiles include securities which pay coupon only where certain conditions relating to equity performance, foreign currency movements, or other factors are met.

Commercial paper represents short term issuances where the funding typically carries a three month term.

Other financial liabilities represent funded swap transactions.

MUSHD loan facility represents senior unsecured intercompany borrowings lent under an uncommitted loan facility which allows the Company to borrow funds from MUSHD.

18 Other liabilities

	2017 £'000	2016 £'000
Payables to structured entities	406,342	205,626
Tax and social security	12,645	23,080
Pension liability (Note 7)	-	7,711
Other creditors	306,421	230,343
	725,408	**466,760**

19 Subordinated liabilities

	2017 £'000	2016 £'000
JPY 24.0 billion floating rate loan due December 2026 at 6-month JPY LIBOR +80bps	158,203	168,628
JPY 20.0 billion floating rate loan due December 2026 at 6-month JPY LIBOR +80bps	131,835	140,523
	290,038	**309,151**

Subordinated loans are agreed between the Company and its immediate parent, MUSHD.

20 Equity instruments

	2017		2016	
	No. '000	**£'000**	**No. '000**	**£'000**
Ordinary shares of £1 each:				
Authorised	2,000,000	2,000,000	2,000,000	2,000,000
Share capital as at 1 January	1,010,611	1,010,611	1,010,611	1,010,611
Allotted, called up and fully paid as at 31 December	**1,010,611**	**1,010,611**	**1,010,611**	**1,010,611**
Additional Tier 1 capital:				
Additional Tier 1 capital as at 1 January		306,979		-
Issued in the year		-		306,979
Additional Tier 1 capital as at 31 December		**306,979**		**306,979**
Total equity instruments		**1,317,590**		**1,317,590**

The Company has one class of ordinary shares which carry no right to fixed income.

On 15 December 2016, the Company issued Additional Tier 1 capital instruments to MUSHD with a value of approximately £307m. The instruments include a contingent conversion feature which has the effect of converting the instruments to ordinary share capital of the Company if a trigger event, being a breach of minimum Common Equity Tier 1 capital ratio, occurs at any time. *The instruments are perpetual and are subordinated to senior creditors and subordinated loan creditors of the Company.* The instruments bear a floating rate of interest. All interest payments are cancellable in certain circumstances, where certain distribution tests are breached, and are non-cumulative.

21 Distributions on equity instruments

On 16 January 2017, the Directors approved the initial coupon payment of £728k on the AT1 capital issued on 15 December 2016 (refer to Note 20 for terms of the issuance).

On 15 July 2017, the Directors approved a coupon payment on the AT1 capital instruments of £4,418k.

On 15 January 2018, the Directors approved a coupon payment on the AT1 capital instruments of £4,273k. The amount has not been accrued in the results for the year ended 31 December 2017 as it was not due at that date.

No ordinary dividends were approved or paid during the year (2016: £ Nil).

22 Report on Directors' remuneration and interests

	2017 £'000	2016 £'000
Short term employment benefits	2,715	3,725
Post employment benefits	31	40
Other long term benefits	1,158	648
Notional share based payments	695	648
Remuneration of key management personnel	**4,599**	**5,061**
Realised MTM / interest on NSUs & other long term benefits	130	(41)
Total remuneration of key management personnel	**4,729**	**5,020**

The number of Directors who were members of the Group defined contribution personal pension plan during the period was 3 (2016: 3).

NSUs are cash settled awards linked to the share price of the ultimate holding company, MUFG. Deferred NSU compensation expense is pro-rated across the entire deferral period. Deferred cash compensation expense is recognised during the period the award is made.

Non-executive Directors provided by other Group companies receive no fees or other remuneration for their services to the Company. The key management are the same personnel as the Directors of the Company.

The emoluments of the highest paid Director were as follows:

	2017 £'000	2016 £'000
Short term employment benefits	1,012	1,247
Post employment benefits	9	13
Other long term benefits	620	365
Notional share based payments	372	365
Remuneration award	**2,013**	**1,990**
Realised MTM / interest on NSUs & other long term benefits	87	(41)
Total remuneration	**2,100**	**1,949**

23 Fair value of financial instruments

The majority of the Company's assets and liabilities are carried on the balance sheet at fair value, in which case fair value is equal to the carrying value.

The following table presents a comparison by category of book amounts and fair value of the Company's financial assets and liabilities for those items which are not carried at fair value on the balance sheet.

	2017		2016	
	Carrying value £'000	Fair value £'000	Carrying value £'000	Fair value £'000
Assets				
Reverse repurchase agreements	130,494	130,415	200,066	200,066
Cash collateral paid to derivative counterparties	2,528,987	2,528,987	2,474,924	2,474,924
Other assets	255,805	255,805	373,469	373,469
Liabilities				
Cash collateral received from derivative counterparties	7,606,270	7,606,270	7,853,174	7,853,174
Other liabilities	725,408	725,408	466,760	466,760
Subordinated liabilities	290,038	292,882	309,151	315,494

23 Fair value of financial instruments (continued)

FX gains of £337m (2016: loss of £1,186m) were recognised on financial assets and liabilities not carried at fair value, driven by revaluation of cash collateral received from derivative counterparties. The currency exposure is economically hedged with instruments held at fair value, with FX gains and losses and associated fair value gains and losses being recognised net in the Income statement as Trading income.

Valuation of financial assets and liabilities

Valuation techniques incorporate assumptions about factors that other market participants would use in their valuations, including interest rate yield curves, exchange rates, volatilities and prepayment and default rates. The Company measures fair value using the following fair value hierarchy that reflects the significance of the inputs used in making measurements:

- Level 1: Quoted market price (unadjusted) in an active market for an identical instrument.
- Level 2: Valuation techniques based on observable inputs, either directly (i.e. as prices) or indirectly (i.e. derived from prices). This category includes instruments valued using quoted market prices in active markets for similar instruments; quoted prices for identical or similar instruments in markets that are considered less than active; or other valuation techniques where all significant inputs are directly or indirectly observable from market data.
- Level 3: Valuation techniques using significant unobservable inputs. This category includes all instruments where the valuation technique includes inputs not based on observable data and the unobservable inputs have a significant effect on the instrument's valuation. This category includes instruments that are valued based on quoted prices for similar instruments where significant unobservable adjustments or assumptions are required to reflect differences between the instruments.

Issued structured notes and certain other hybrid instrument liabilities are designated at fair value. The spread applied to these instruments is derived from the spreads at which the Company issues structured notes. The change in fair value due to credit risk on these instruments is not significant (2016: not significant).

The fair value of certain financial instruments is measured using valuation techniques that are determined in full or partly on assumptions that are not supported by observable market prices. The effect of changing these assumptions to a range of reasonably possible alternative assumptions would provide a range from £32.5 million (2016: £5.1 million) lower to £22.6 million (2016: £26.1 million) higher than the fair value recognised in the financial statements for these assets and liabilities, with the current year range driven by increased volume of equity financing trades. It should be noted that for financial instruments whose valuations are not supported by observable market prices, profits are reserved at inception and these have not been adjusted in making this calculation.

The movements in balances of level 3 items are detailed on page 46.

23 Fair value of financial instruments (continued)

	2017			
	Level 1 £'000	**Level 2 £'000**	**Level 3 £'000**	**Total £'000**
Assets				
Trading portfolio financial assets	5,537,102	2,921,558	-	8,458,660
Reverse repurchase agreements - fair value	-	22,459,995	-	22,459,995
Cash collateral on securities borrowed	-	6,468,603	-	6,468,603
Financial instruments available for sale	577,800	240,808	131	818,739
Derivative financial instruments	132	13,032,826	412,617	13,445,575
Equity finance assets	-	488,261	-	488,261
	6,115,034	**45,612,051**	**412,748**	**52,139,833**
Liabilities				
Trading portfolio financial liabilities	5,595,539	172,308	-	5,767,847
Repurchase agreements - fair value	-	21,990,927	-	21,990,927
Cash collateral on securities lent	-	1,772,714	-	1,772,714
Derivative financial instruments	3,900	11,336,494	423,002	11,763,396
Financial liabilities designated at fair value	-	4,395,885	269,128	4,665,013
	5,599,439	**39,668,328**	**692,130**	**45,959,897**

	2016			
	Level 1 £'000	**Level 2 £'000**	**Level 3 £'000**	**Total £'000**
Assets				
Trading portfolio financial assets	3,294,091	2,064,918	-	5,359,009
Reverse repurchase agreements - fair value	-	42,384,371	-	42,384,371
Cash collateral on securities borrowed	-	7,824,309	-	7,824,309
Financial instruments available for sale	1,029,824	727,432	125	1,757,381
Derivative financial instruments	1,104	18,995,010	300,866	19,296,980
Equity finance assets	-	485,331	-	485,331
	4,325,019	**72,481,371**	**300,991**	**77,107,381**
Liabilities				
Trading portfolio financial liabilities	5,381,429	165,273	-	5,546,702
Repurchase agreements - fair value	-	41,936,030	-	41,936,030
Cash collateral on securities lent	-	444,514	-	444,514
Derivative financial instruments	107,759	17,887,745	401,672	18,397,176
Financial liabilities designated at fair value	-	4,083,004	480,533	4,563,537
	5,489,188	**64,516,566**	**882,205**	**70,887,959**

During the year, the Company made a levelling reassessment for a portfolio of listed futures and options. The illiquid nature of the positions resulted in wide bid-offer spreads with a skewed mid-point, meaning the unadjusted exchange price does not accurately reflect traded prices. The impact of this is a transfer of £0.5m assets and £62.1m liabilities from Level 1 to Level 2.

23 Fair value of financial instruments (continued)

The table below shows a reconciliation from the beginning balances to the end balances for the fair value of instruments in level 3 of the fair value hierarchy. This does not include movements in level 1 or level 2 derivatives that are also used to hedge the level 3 assets and liabilities.

	Derivative assets £'000	Available for sale securities £'000	Derivatives liabilities £'000	Financial liabilities designated at fair value £'000
Opening balance 1 January 2017	300,866	125	(401,672)	(480,533)
Total gains/(losses) in profit and loss	146,834	-	7,923	(9,913)
Total gains in reserves	-	6	-	-
Purchases	-	-	-	-
Issues	-	-	-	(38,002)
Settlements	(117,883)	-	19,015	42,764
Transfers into level 3	82,801	-	(52,485)	(7,384)
Transfers from level 3	-	-	4,217	223,940
Closing balance 31 December 2017	**412,617**	**131**	**(423,002)**	**(269,128)**

Unrealised gains or losses for the year included in income statement for assets and liabilities held at the end of financial year:

- Net trading income	158,463	-	(36,267)	(5,887)

"Transfers into level 3" derivatives are driven by a callable accreting swaps portfolio. This was transferred into level 3 following an increase in the degree of valuation judgement required within the valuation model and associated uncertainty provisions.

"Transfers from level 3" are driven by structured notes which have been reclassified into level 2 of the hierarchy. The notes contain exotic embedded derivatives, primarily linked to foreign exchange rates which drive the returns and valuation of the notes. During the period, there has been an increase in the observability of the key inputs to the valuation models and a corresponding decrease in the significance of the unobservable valuation inputs.

Financial instruments valued using models with unobservable inputs

The amount that has yet to be recognised in the Company income statement relating to the difference between the fair value at initial recognition (the transaction price) and the amount that would have arisen had valuation techniques used for subsequent measurement been applied at initial recognition, less subsequent releases, is as follows:

	2017 £'000	2016 £'000
Unamortised balance at 1 January	104	7,288
Deferral on new transactions	-	-
Amortised to the profit and loss account during the financial year	(104)	(7,184)
Unamortised balance at 31 December	**-**	**104**

Financial assets designated at fair value

The Company did not have any financial assets designated at fair value at 31 December 2017 (2016: nil).

23 Fair value of financial instruments (continued)

Significant unobservable inputs

The disclosures below describe the valuation techniques and significant unobservable inputs for assets and liabilities classified as Level 3 along with the range of values used for those significant unobservable inputs. Level 3 financial liabilities designated at fair value totalling £269m (2016: £480m) contain embedded derivatives with inputs represented by the Interest rate, Foreign exchange and Equity derivatives described in the table below.

	Total assets £'000	Total liabilities £'000	Valuation technique(s)	Significant unobservable inputs	Range Min	Range Max	Units
Interest rate derivatives	116,648	(68,769)	Option model	IR - IR Correlation	43.16	50.12	%
				FX - IR Correlation	46.40	46.40	%
				Option volatility	13.44	100.00	%
				Prepayment probability	100.00	100.00	%
Foreign exchange derivatives	61,605	(130,864)	Option model	IR - IR Correlation	40.26	73.95	%
				FX - IR Correlation	46.40	50.65	%
				Correlation - underlying assets	85.00	85.00	%
				Option volatility	10.33	16.22	%
Equity derivatives	45,015	(33,549)	Option model	Equity - IR Correlation	37.13	37.13	%
				Equity - FX Correlation	7.00	7.00	%
				Correlation - underlying assets	76.00	76.00	%
			Discounted cash flows	Term of Litigation swap	2.00	2.00	Year
Commodities	189,349	(189,820)	Option model	Commodity - IR Correlation	25.00	75.00	%
				Commodity - Gas swap rate	2.73	4.24	%
	412,617	**(423,002)**					

The following provides a summary description of significant unobservable inputs included in the table above:

- Correlation is a measure of the relationship between the movements of two variables (i.e. how much the change in one variable may be linked to the change in the other variable). Correlation is often an input into valuation of derivative contracts with more than one underlying risk. A significant increase in correlation in isolation can result in a movement in fair value that is favourable or unfavourable depending on the specific terms of the instrument.

- Prepayment probability is the probability of voluntary, unscheduled repayments by a borrower. Unscheduled prepayment affects the average life of transactions by altering the timing of principal repayment and the amount of interest earned. A significant increase in a prepayment probability can result in a movement in fair value that is favourable or unfavourable depending on the specific terms of the financial contract.

- Option volatility is a measure of the degree of variation in price movements for a given derivative underlying, and therefore represents an estimate of how much a particular underlying instrument, parameter or index could change on average over time. In general, a significant increase in volatility in isolation will result in an increase in fair value for the holder of a simple option.

- Term of litigation swap relates to a series of swaps linked to an asset which is affected by a legal case, where the payments under the swap terminate soon after the litigation ends. The term of the swap is therefore difficult to quantify and needs to be estimated from available information and legal opinion. A decrease in the expectation of the term of the swap would generally result in an unfavourable move in the fair value.

24 Obligations under finance leases

	2017 £'000	2016 £'000
Minimum lease payments:		
Within 1 year	936	258
Between 1 and 5 years	1,316	861
After 5 years	-	-
Amounts payable under finance leases	**2,252**	**1,119**
Add: future financing income	472	33
Present value of lease obligations	**2,724**	**1,152**
Amounts payable under finance leases:		
Within 1 year	1,240	274
Between 1 and 5 years	1,484	878
After 5 years	-	-
Present value of lease obligations	**2,724**	**1,152**

The Company leases certain of its fixtures and equipment under finance leases. The average lease term is 5 years. For the year ended 31 December 2017, the average effective borrowing rate was (12.6)% (2016: (1.44)%). Interest rates are fixed at the contract date.

All leases are on a fixed repayment basis and no arrangements have been entered into for contingent rental payments. All lease obligations are denominated in pounds sterling.

The fair value of the Company's lease obligations is approximately equal to their carrying value. The Company's obligations under finance leases are secured by the lessor's rights over the leased assets disclosed in Notes 13 and 14.

25 Post-balance sheet events

There have been no material post-balance sheet events which would require disclosure or adjustment to the 31 December 2017 Financial Statements. An AT1 coupon payment of £4,273k was approved on 15 January 2018 (refer to Note 21).

26 Collateral

Assets are pledged as collateral to secure liabilities under repurchase agreements, securities lending agreements, borrowing transactions, to note holders as part of structuring transactions and agreements for derivative transactions. The following table summarises the nature and carrying amount of the assets pledged as security against these liabilities:

	2017 £'000	2016 £'000
Trading securities	4,501,193	2,946,541
Investment securities	386,562	1,020,936
Total assets pledged as collateral	**4,887,755**	**3,967,477**

Under certain transactions, including reverse repurchase agreements and stock borrowing transactions, the Company is allowed to resell or repledge the collateral held. The fair value of collateral accepted with the right to repledge to others was as follows:

	2017		2016	
	Fair Value £'000	Sold or repledged £'000	Fair Value £'000	Sold or repledged £'000
Accepted collateral	50,869,392	46,259,575	65,542,276	60,956,153

These balances represent substantially all of the collateral received by the Company in relation to assets. The Company has the obligation to return the collateral on the maturity date of the secured transaction. The process by which assets are pledged as collateral and accepted as collateral is conducted under the terms that are usual and customary to the business stated.

26 Collateral (continued)

Transferred Assets

The Company enters into transactions in the normal course of business by which it transfers recognised financial assets to third parties or to special purpose entities, but the transfer does not qualify for de-recognition as stated in the accounting policies. The Company will continue to recognise financial assets transferred when it retains control of the security, retains rights to receive cash flows from the assets, and substantially all the risks and rewards of ownership. The carrying amount of debt securities that have been transferred to special purpose entities but do not meet the criteria for de-recognition are summarised below:

	2017 £'000	2016 £'000
Securities transferred to special purpose entities	41,795	84,081

Collateral Management of Repurchase Agreements

Securities purchased under agreements to resell ("reverse repurchase agreements") and securities sold under agreements to repurchase ("repurchase agreements") are mainly collateralised by highly rated credit bonds (predominantly government and corporate bonds). The repurchase agreements are treated as collateralised financing transactions and are carried at the contract amounts at which the securities will subsequently be reacquired or resold as specified in the respective agreements. It is the Company's policy to generally take possession of securities purchased under agreements to resell at the time such agreements are made. The Company's agreements with counterparties contain provisions allowing for additional collateral to be obtained, or excess collateral returned, based on market valuations of such collateral. The Company re-values the collateral underlying its repurchase and reverse repurchase agreements on a daily basis. In the event the market value of such securities falls below the related agreement to resell at contract amount plus accrued interest, the Company will generally request additional collateral.

Unconsolidated structured entities in which the Company has an interest

The Company is involved with various special purpose entities in the normal course of business. These have been established as structured entities such that voting or similar rights are not the deciding factor in determining control of the entity.

The structured entities are typically asset repackaging transactions established to source funding, purchase credit protection or provide returns to investors that are not otherwise readily available in the market. The principle risk to the structure is the credit risk of the securities acting as collateral to the investors who retain the risk and rewards.

The following tables represent the total assets, maximum exposure to loss and assets and liabilities which relate to the Company's interest in non-consolidated special purpose vehicles ("SPVs"). Maximum exposure is determined by the carrying amount of any on-balance sheet assets net of any recourse liabilities, where applicable.

As at 31 December 2017	SPVs for structured financing £'000	Repackaged instruments £'000	Other £'000	Total £'000
Trading portfolio financial assets	-	409,170	-	409,170
Derivative financial instruments	1,727,992	129,965	202,276	2,060,233
Reverse repurchase agreements	-	455,534	671,558	1,127,092
Other assets	15,322	-	1,785	17,107
Total Assets	**1,743,314**	**994,669**	**875,619**	**3,613,602**
Derivative financial instruments	43,027	10,284	21,911	75,222
Financial liabilities designated at fair value	-	688,002	-	688,002
Other liabilities	-	239,270	221,469	460,739
Derivative cash collateral received	-	26,474	33,773	60,247
Total Liabilities	**43,027**	**964,030**	**277,153**	**1,284,210**
Maximum Exposure	**1,728,755**	**821,301**	**641,479**	**3,191,535**

26 Collateral (continued)

As at 31 December 2016	SPVs for structured financing £'000	Repackaged instruments £'000	Other £'000	Total £'000
Trading portfolio financial assets	-	205,453	-	205,453
Derivative financial instruments	2,022,323	154,580	208,072	2,384,975
Reverse repurchase agreements	3,638	174,136	554,162	731,936
Total Assets	**2,025,961**	**534,169**	**762,234**	**3,322,364**
Derivative financial instruments	105,396	38,437	1,978	145,811
Financial liabilities designated at fair value	-	607,794	-	607,794
Other liabilities	-	173,449	111,266	284,715
Derivative cash collateral received	48,069	-	29,066	77,135
Total Liabilities	**153,465**	**819,680**	**142,310**	**1,115,455**
Maximum Exposure	**1,977,892**	**360,720**	**623,951**	**2,962,563**

27 Guarantees, commitments and contingent liabilities

At the year end, the Company was committed to provide collateralised financing facilities in favour of two investment grade financial counterparties. The facilities are provided in major currencies and total £186.0 million (2016: £204.5 million) equivalent; none had been drawn against at year end. The facilities are required to be fully collateralised from a range of pre-defined debt securities limited to US Treasuries and highly rated government or supra-national bonds.

At the date of signing this report, the above two agreements were extended until 31 January 2019.

28 Contractual maturity analysis

The breakdown of financial liabilities by contractual maturity, which is based on the contractual terms, is shown in the table below. The balances do not agree directly to the balances in the balance sheet as the table incorporates contractual cash flows on an undiscounted basis. The repurchase agreement balances are presented on a gross basis, not taking account of any balances which have been offset in the balance sheet. Derivative contracts are reflected as on demand at their fair value. The subordinated liabilities bear interest at variable rates which are not known until specified fixing dates have occurred.

	2017					
	On demand £'000	Due within 3 months £'000	Due between 3 and 12 months £'000	Due between 1 and 5 years £'000	Over 5 years £'000	Total £'000
Deposits by banks	88,311	-	-	-	-	88,311
Trading portfolio financial liabilities	5,767,847	-	-	-	-	5,767,847
Repurchase agreements	700,499	31,969,119	1,408,147	668,136	-	34,745,901
Cash collateral on securities lent	392,671	1,415,773	-	-	-	1,808,444
Cash collateral received from derivatives counterparties	7,606,270	-	-	-	-	7,606,270
Derivatives	11,763,396	-	-	-	-	11,763,396
Financial liabilities designated at fair value	-	1,497,658	1,582,657	939,793	734,476	4,754,584
Other liabilities	648,336	29,308	6,324	41,440	-	725,408
Subordinated liabilities	-	-	2,444	10,779	303,799	317,022
	26,967,330	**34,911,858**	**2,999,572**	**1,660,148**	**1,038,275**	**67,577,183**

28 Contractual maturity analysis (continued)

	2016					
	On demand £'000	Due within 3 months £'000	Due between 3 and 12 months £'000	Due between 1 and 5 years £'000	Over 5 years £'000	Total £'000
Deposits by banks	72,392	-	-	-	-	72,392
Trading portfolio financial liabilities	5,546,702	-	-	-	-	5,546,702
Repurchase agreements	977,820	51,287,478	1,223,320	334,196	-	53,822,814
Cash collateral on securities lent	444,514	-	-	-	-	444,514
Cash collateral received from derivatives counterparties	7,853,174	-	-	-	-	7,853,174
Derivatives	18,397,176	-	-	-	-	18,397,176
Financial liabilities designated at fair value	-	789,211	1,822,360	1,193,463	945,785	4,750,819
Other liabilities	388,985	42,882	6,235	28,658	-	466,760
Subordinated liabilities	-	-	2,537	11,012	327,142	340,691
	33,680,763	**52,119,571**	**3,054,452**	**1,567,329**	**1,272,927**	**91,695,042**

The Company holds liquid assets comprising cash and cash equivalents and investment securities for which there is an active and liquid market. These assets can be readily sold to meet liquidity requirements.

Financial liabilities designated at fair value include certain note issuances with structured payment profiles. The notes are issued across a range of currencies and interest rate profiles, with the most prevalent being JPY floating rate notes. The Company issue these notes to raise term funding and satisfy investor demand, and carries them at fair value through profit and loss. Some of the notes may be redeemed prior to maturity subject to certain knock-out events, at the option of the issuer or holder of the debt. These factors are contractually specified at the point of issuance.

29 Operating lease arrangements

The Company as lessee

	2017 £'000	2016 £'000
Lease payments under operating leases recognised as an expense in the year	3,521	844

At the balance sheet date, the Company had outstanding commitments for future minimum lease payments under non-cancellable operating leases, which fall due as follows:

	2017 £'000	2016 £'000
Buildings		
Within 1 year	4,170	4,170
Between 1 - 2 years	4,170	4,170
Between 2 - 5 years	12,510	12,510
After 5 years	29,190	33,360
	50,040	**54,210**

Operating lease payments represent rentals payable by the Company for certain office properties and data centres. Building leases are negotiated for an average term of 20 years.

30 Offsetting financial assets and financial liabilities

In accordance with IAS 32 Financial Instruments: Presentation, the Company reports financial assets and financial liabilities on a net basis on the balance sheet only if there is a legally enforceable right to set off the recognised amounts and there is intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. The following table shows the impact of netting arrangements on:

- All financial assets and liabilities that are reported net on the balance sheet; and
- All derivative financial instruments, reverse repurchase and repurchase agreements and other similar secured lending and borrowing agreements that are subject to enforceable master netting arrangements or similar agreements, but do not qualify for balance sheet netting.

The table identifies the amounts that have been offset in the balance sheet and also those amounts that are covered by enforceable netting arrangements (offsetting arrangements and financial collateral) but do not qualify for netting under the requirements of IAS 32 described above.

The net amounts presented in the following table are not intended to represent the Company's actual exposure to credit risk, as a variety of credit mitigation strategies are employed in addition to netting and collateral arrangements.

	Amounts subject to enforceable netting arrangements								
	Effects of offsetting on balance sheet			Related amounts not offset			Exposure		
	Gross amounts £'000	Amounts offset £'000	Net amounts on balance sheet £'000	Financial instru-ments £'000	Cash collateral £'000	Financial collateral £'000	Net amount £'000	Not subject to enforce-able netting £'000	Balance sheet total £'000
As at 31 December 2017									
Derivative financial assets	12,582,060	157,787	12,424,273	7,611,830	1,757,407	3,065	3,051,971	1,021,302	13,445,575
Reverse repurchase agreements	35,385,164	13,183,953	22,201,211	2,585,193	109,389	19,461,670	44,959	389,278	22,590,489
Secured lending	6,423,451	-	6,423,451	223,352	-	6,166,497	33,602	45,152	6,468,603
Total Assets	54,390,675	13,341,740	41,048,935	10,420,375	1,866,796	25,631,232	3,130,532	1,455,732	42,504,667
Derivative financial liabilities	11,353,752	149,899	11,203,853	7,611,830	2,341,586	36,279	1,214,158	559,544	11,763,397
Repurchase agreements	34,733,269	12,758,403	21,974,866	2,585,193	29,338	19,335,784	24,551	16,061	21,990,927
Secured borrowing	1,772,714	-	1,772,714	223,352	-	1,538,795	10,567	-	1,772,714
Total Liabilities	47,859,735	12,908,302	34,951,433	10,420,375	2,370,924	20,910,858	1,249,276	575,605	35,527,038
As at 31 December 2016									
Derivative financial assets	41,177,623	23,225,549	17,952,074	12,557,985	1,459,756	36,010	3,898,370	1,344,906	19,296,980
Reverse repurchase agreements	54,199,409	11,862,053	42,337,356	4,025,367	79,090	38,182,719	50,180	247,081	42,584,437
Secured lending	7,475,898	-	7,475,898	48,539	-	7,373,924	53,435	348,411	7,824,309
Total Assets	102,852,977	35,087,602	67,765,375	16,631,891	1,538,846	45,592,653	4,001,985	1,940,398	69,705,773
Derivative financial liabilities	40,865,333	23,428,106	17,437,227	12,557,985	2,274,896	855,755	1,748,637	959,949	18,397,176
Repurchase agreements	53,791,141	11,862,053	41,929,088	4,025,367	-	37,862,019	41,702	6,942	41,936,030
Secured borrowing	444,514	-	444,514	48,539	-	391,136	4,839	-	444,514
Total Liabilities	95,101,034	35,290,159	59,810,875	16,631,891	2,274,896	39,108,910	1,795,178	966,891	60,777,766

31 Related party transactions

Balances and transactions between the Company and related parties are disclosed below.

	2017			
	Parent Company £'000	MUFG £'000	Other Related Parties £'000	Total £'000
Income	0	89,155	2,966	92,121
Expenses	12,200	11,732	2,502	26,434
Total assets	4,010	10,274,158	251,762	10,529,930
Total liabilities	1,210,581	8,612,924	261,320	10,084,825

	2016			
	Parent Company £'000	MUFG £'000	Other Related Parties £'000	Total £'000
Income	84	58,925	35	59,044
Expenses	17,831	5,652	105	23,588
Total assets	3,702	19,585,688	471,878	20,061,268
Total liabilities	1,959,789	9,708,696	379,079	12,047,564

31 Related party transactions (continued)

All related parties are wholly owned subsidiaries of MUFG, with the exception of Morgan Stanley Group companies, which are presented as 'Other Related Parties' due to their affiliate status with MUFG.

Transactions executed with related parties are entered into at market price on an arm's length basis. No provisions have been made for doubtful debts in respect of the amounts owed by related parties.

Income includes fee allocations from the Equity and Structuring businesses. Expenses includes interest for subordinated loans and management fees paid to the parent company as well as fees paid for a keepwell and guarantees in place between MUS(EMEA), BTMU and MUFG. Total assets include the credit derivative, which is a BTMU guarantee, referred to in Note 11.

There are no material related party transactions with key management, and persons connected with them, other than remuneration disclosed in Note 22.

32 Group information

MUFG Securities EMEA plc is a company incorporated in the United Kingdom under the Companies Act. The address of the registered office is given on page 2. The principal activities of the Company and the nature of the Company's operations are set out in the Strategic Report on pages 1 to 2.

The Company's immediate parent undertaking is Mitsubishi UFJ Securities Holdings Co., Ltd., a company registered in Japan. The Company's ultimate parent company and ultimate controlling party is Mitsubishi UFJ Financial Group, incorporated in Japan.

The audited consolidated financial statements of Mitsubishi UFJ Securities Holdings Co., Ltd. are made available to the public annually and may be obtained from its registered office at:

Mitsubishi UFJ Securities Holdings Co., Ltd.
5-2, Marunouchi 2-chome
Chiyoda-ku
Tokyo 100-0005
Japan