

Governance

	Page
Our Board	58
Corporate governance	63
Report of the Group Nominations and Governance Committee	69
Report of the Group Audit Committee	71
Report of the Board Risk Committee	79
Report of the Sustainable Banking Committee	85
Directors' remuneration report	88
Other Remuneration Disclosures	109
Compliance report	112
Report of the directors	115
Statement of directors' responsibilities	122

Our Board

Chairman



Howard Davies (age 66)

Nationality: British

Date of appointment: 14 July 2015 (Board),
1 September 2015 (Chairman)

Experience: Howard was Deputy Governor of the Bank of England from 1995 to 1997 and Chairman of the UK Financial Services Authority from 1997 to 2003. Howard was Director of the London School of Economics and Political Science from 2003 until May 2011. He is also Professor of Practice at the Paris Institute of Political Science (Sciences Po).

Howard was chair of the UK Airports Commission between 2012 and 2015 and is also the author of several books on financial subjects.

External appointment(s):

Independent director of Prudential plc and chair of the Risk Committee
Member of the Regulatory and Compliance Advisory Board of Millennium Management LLC
Chair of the International Advisory Council of the China Securities Regulatory Commission
Member of the International Advisory Council of the China Banking Regulatory Commission
Chairman of the London Library Trustees

Committee membership(s):

Group Nominations and Governance Committee (Chairman)

Executive directors

Chief Executive



Ross McEwan (age 59)

Nationality: New Zealand

Date of appointment: 1 October 2013

Experience: Ross became Chief Executive of The Royal Bank of Scotland Group in October 2013. Between August 2012 and September 2013, he was Chief Executive Officer for UK Retail, joining from Commonwealth Bank of Australia where he was Group Executive for Retail Banking Services for five years. Prior to this he was Executive General Manager with responsibility for the branch network, contact centres and third party mortgage brokers.

Ross has more than 25 years experience in the finance, insurance and investment industries. Prior to Commonwealth Bank of Australia, he was Managing Director of First NZ Capital Securities. He was also Chief Executive of National Mutual Life Association of Australasia Ltd/AXA New Zealand Ltd. Ross has an MBA from Harvard.

External appointment(s):

None

Committee membership(s):

Executive Committee (Chairman)

Chief Financial Officer



Ewen Stevenson (age 50)

Nationality: British/New Zealand

Date of appointment: 19 May 2014

Experience: Prior to his current role, Ewen was at Credit Suisse for 25 years where he was latterly co-Head of the EMEA Investment Banking Division and co-Head of the Global Financial Institutions Group. He has over 20 years of experience advising the banking sector while at Credit Suisse.

Ewen has a Bachelor of Commerce and Administration majoring in Accountancy and a Bachelor of Law from Victoria University of Wellington, New Zealand.

External appointment(s):

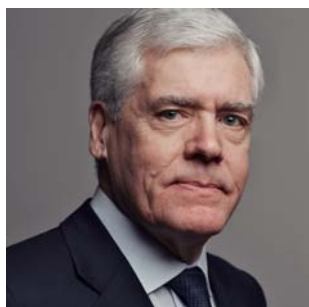
None

Committee membership(s):

Executive Committee
US Risk Committee

Our Board

Independent non-executive directors



Sandy Crombie (age 68)

Nationality: British

Date of appointment: 1 June 2009

(Senior Independent Director)

Experience: Sandy spent his entire full-time career with Standard Life plc, retiring as Group Chief Executive. An actuary, he has served his profession in a variety of roles and has also served as a director of the Association of British Insurers.

Sandy has had a variety of cultural and community roles, and was previously Chairman of Creative Scotland, Chairman of the Edinburgh World City of Literature Trust and vice-Chairman of the Royal Conservatoire of Scotland.

External appointment(s):

President of the Cockburn Association

Committee membership(s):

Group Performance and Remuneration Committee (Chairman)
Group Audit Committee
Group Nominations and Governance Committee
GRG Board Oversight Committee



Frank Dangeard (age 59)

Nationality: French

Date of appointment: 16 May 2016

Experience: Previously, Frank served as a non-executive director of Crédit Agricole CIB, EDF, Home Credit, Orange, Sonaecom SGPS, and as Deputy Chairman and acting Chairman of Telenor ASA. During his executive career he held various roles at Thomson S.A., including Chairman and Chief Executive Officer, and was Deputy Chief Executive Officer of France Telecom. Prior to that he was Chairman of SG Warburg France and a Managing Director of SG Warburg.

Frank is a graduate of HEC and IEP in Paris and of the Harvard Law School in the US.

External appointment(s):

Non-executive director of the RPX Corporation

Non-executive director of Symantec Corporation

Committee membership(s):

Board Risk Committee



Alison Davis (age 55)

Nationality: British/USA

Date of appointment: 1 August 2011

Experience: Previously, Alison served as a director of City National Bank, First Data Corporation, Xoom, Diamond foods and chair of the board (and as Non-executive director) of LECG Corporation. She has also worked at McKinsey & Company, AT Kearney, as Chief Financial Officer at Barclays Global Investors (now BlackRock) and as managing partner of Belvedere Capital, a private equity firm focused on buy-outs in the financial services sector.

Alison is a graduate of Cambridge University and Stafford Business School.

External appointment(s):

Non-executive director and member of the compensation and audit committees of Unisys Corporation

Non-executive director, and member of the audit committee of Fiserv Inc

Non-executive director and chair of the audit committee of Ooma Inc

Committee membership(s):

Group Nominations and Governance Committee
Group Performance and Remuneration Committee
Sustainable Banking Committee

Our Board

Independent non-executive directors



Morten Friis (age 64)

Nationality: Norwegian

Date of appointment: 10 April 2014

Experience: Previously, Morten had a 34 year financial services career and held various roles at Royal Bank of Canada and its subsidiaries including Associate Director at Orion Royal Bank, Vice President, Business Banking and Vice President, Financial Institutions. In 1997, he was appointed as Senior Vice President, Group Risk Management and served as the Chief Credit Officer then Chief Risk Officer from 2004 to 2014. He was also previously a Director of RBC Bank (USA), Westbury Life Insurance Company, RBC Life Insurance Company and of RBC Dexia Investor Services Trust Company.

External appointment(s):

Member of the Board of Directors of The Canadian Institute for Advanced Research
Member of the Board of Directors of the Harvard Business School Club of Toronto
Non-executive director of Jackson National Life Insurance Company

Committee membership(s):

Group Audit Committee
Board Risk Committee
US Risk Committee (Chairman)



Robert Gillespie (age 61)

Nationality: British

Date of appointment: 2 December 2013

Experience: Robert began his career with Price Waterhouse (now PricewaterhouseCoopers) where he qualified as a chartered accountant. He then moved into banking joining SG Warburg, specialising in corporate finance, and was appointed as Co-Head and Managing Director of its US investment banking business in 1989. Following the acquisition in 1995 of Warburg by Swiss Bank Corporation (which subsequently merged with UBS), he then held the roles of Head of UK Corporate Finance, Head of European Corporate Finance and Co-Head of its global business and CEO of the EMEA region. He relinquished his management roles at the end of 2005, and was appointed Vice Chairman of UBS Investment Bank. Robert left UBS to join Evercore Partners, from where he was seconded to the UK Panel on Takeovers and Mergers, as Director General, from 2010 to 2013.

External appointment(s):

Independent board director at Ashurst LLP
Chairman of Council at the University of Durham
Chairman of the Boat Race Company Limited
Director of Social Finance Limited

Committee membership(s):

Group Nominations and Governance Committee
Group Performance and Remuneration Committee
Sustainable Banking Committee
GRG Board Oversight Committee



Penny Hughes, CBE (age 57)

Nationality: British

Date of appointment: 1 January 2010

Experience: Previously a non-executive director and Chairman of the corporate compliance and responsibility committee of Wm Morrison Supermarkets plc. Other former non-executive directorships include Skandinaviska Enskilda Banken AB, Home Retail Group plc, Vodafone Group plc, Reuters Group PLC, Cable & Wireless Worldwide plc and The Gap Inc. Penny spent the majority of her executive career at Coca-Cola where she held a number of leadership positions, latterly as President, Coca-Cola Great Britain and Ireland.

External appointment(s):

Non-executive Chairman of The Gym Group plc. Also chair of the nominations and member of the audit, risk and remuneration committees
Non-executive director and member of the audit and nomination committees of SuperGroup plc

Committee membership(s):

Sustainable Banking Committee (Chairman)
Board Risk Committee
GRG Board Oversight Committee

Our Board

Independent non-executive directors



Brendan Nelson (age 67)

Nationality: British

Date of appointment: 1 April 2010

Experience: Brendan was global Chairman, financial services for KPMG. He previously held senior leadership roles within KPMG including as a member of the KPMG UK board from 1999 to 2006 and as vice-Chairman from 2006 until his retirement in 2010. He was Chairman of the Audit Committee of the Institute of Chartered Accountants of Scotland from 2005 to 2008. President of the Institute of Chartered Accountants of Scotland 2013/14.

External appointment(s):

Non-executive director and Chairman of the audit committee of BP plc
Member of the Financial Reporting Review Panel

Committee membership(s):

Group Audit Committee (Chairman)
Group Nominations and Governance Committee
Board Risk Committee
GRG Board Oversight Committee (Chairman)



Baroness Noakes, DBE (age 67)

Nationality: British

Date of appointment: 1 August 2011

Experience: Baroness Noakes is an experienced director on UK listed company boards with extensive and varied political and public sector experience. A qualified chartered accountant, she previously headed KPMG's European and International Government practices and has been President of the Institute of Chartered Accountants in England and Wales. She was appointed to the House of Lords in 2000 and has served on the Conservative front bench in various roles including as shadow treasury minister between 2003 and May 2010. Previously held non-executive roles on the Court of the Bank of England, Hanson, ICI, Severn Trent, Carpetright, John Laing and SThree.

External appointment(s):

Deputy Chairman, Ofcom

Committee membership(s):

Board Risk Committee (Chairman)
Group Audit Committee
GRG Board Oversight Committee
US Risk Committee



Mike Rogers (age 52)

Nationality: British

Date of appointment: 26 January 2016

Experience: Mike has extensive experience in retail banking and financial services. Mike joined Barclays in 1986 where he undertook a variety of roles in the UK and overseas across business banking, wealth management and retail banking. Mike was Managing Director of Small Business, Premier Banking and UK Retail Banking and was latterly Chief Executive of Liverpool Victoria Group for 10 years.

External appointment(s):

None

Committee membership(s):

Group Performance and Remuneration Committee
Sustainable Banking Committee

Our Board

Chief Governance Officer and Board Counsel



Aileen Taylor (age 44)

Nationality: British

Date of appointment: 1 May 2010
(Company Secretary)

Experience: A qualified solicitor, Aileen joined RBS in 2000. She was appointed Deputy Group Secretary and Head of Group Secretariat in 2007, and prior to that held various legal, secretariat and risk roles including Head of External Risk (Retail), Head of Regulatory Risk (Retail Direct) and Head of Legal and Compliance (Direct Line Financial Services).

Aileen is a fellow of the Chartered Institute of Bankers in Scotland and a member of the European Corporate Governance Council. She is also a member of the FCA's Listing Authority Advisory Panel.

Executive Committee

The Board is supported by the Executive Committee comprising the executive directors and other senior executives. Details of the composition of the Executive Committee and biographies of its members can be found at [rbs.com>about us>board and governance>ceo and board>executive committee](https://www.rbs.com/about-us/board-and-governance/ceo-and-board/executive-committee).

Corporate governance

Chairman's introduction

I am pleased to introduce the corporate governance report. The following report provides an overview of key roles and responsibilities of the Board, and sets out in greater detail how the Board spent its time in 2016. Board effectiveness and performance evaluation are also covered, as well as an overview of how we communicate with shareholders.

As mentioned in my Chairman's Statement on page 6, the Board has considered a number of key strategic, financial, regulatory and litigation matters during 2016.

Understandably, capital strategy and planning remains a priority for the Board. The Board has continued to provide detailed oversight of litigation and conduct matters, particularly the FCA review of the treatment of SME customers, shareholder litigation and RMBS litigation. The divestment of Williams & Glyn; the implications of the EU Referendum result; and the Transformation agenda were all key strategic challenges deliberated by the Board this year. The Board continues to monitor steps being taken to drive cultural change, including risk culture, and ensuring that the right culture and values are embedded throughout the organisation. The Board has considered the preparations for the implementation of ring-fencing and this will be an area of continued focus in 2017.

On 7 March 2016, the PRA and FCA's Senior Managers' Regime came into effect which, alongside the PRA and FCA's new Certification and Conduct Rules regimes, is aimed at strengthening personal accountability and conduct within banking. The Senior Managers' Regime required us to identify those senior executives and board members (referred to as Senior Managers) who would be allocated specific regulatory responsibilities under the Senior Managers' Regime. The Board has received training and ongoing support to ensure that those members who are Senior Managers are able to demonstrate their compliance with the relevant regulatory requirements.

I and my fellow directors are committed to observing high standards of corporate governance, integrity and professionalism. Our statement of compliance with the UK Corporate Governance Code (the Code) can be found on page 112.

I would like to take this opportunity to thank my fellow Directors for their continued commitment and dedication throughout 2016.

Howard Davies, Chairman of the Board

The Board

The Board has twelve directors comprising the Chairman, two executive directors and nine independent non-executive directors, one of whom is the Senior Independent Director.

Biographies for each director and details of which Board committees they are members of can be found on pages 58 to 61. The Board considers that the Chairman was independent on appointment and that all non-executive directors are independent for the purposes of the Code.

Board changes

Mike Rogers was appointed as a non-executive director on 26 January 2016. Mike was appointed as a member of the Sustainable Banking Committee with effect from 25 April 2016, and a member of the Group Performance and Remuneration Committee with effect from 1 January 2017. Frank Dangeard was appointed as a non-executive director on 16 May 2016 and as a member of the Board Risk Committee on 4 August 2016.

Roles and responsibilities

The Board

The Board is collectively responsible for the long-term success of RBS and delivery of sustainable shareholder value. The Board's terms of reference include a formal schedule of matters specifically reserved for the Board's decision and are reviewed at least annually. The terms of reference are available at rbs.com/about.

As mentioned above a number of board members have been designated as "Senior Managers" under the PRA and FCA's Senior Managers' Regime. The role profiles of relevant directors have been updated to reflect their regulatory responsibilities and they receive ongoing support to ensure they can demonstrate the reasonable steps they have taken to meet their responsibilities.

Chairman

The role of Chairman is distinct and separate from that of the Chief Executive and there is a clear division of responsibilities with the Chairman leading the Board and the Chief Executive managing RBS business day to day.

The Chairman's key responsibilities are to:

- provide strong and effective leadership to the Board;
- ensure the Board is structured effectively, observes the highest standards of integrity and corporate governance, and sets the tone from the top in terms of culture and values;
- build an effective and complementary Board with an appropriate balance of skills and personalities, and as Chairman of the Group Nominations and Governance Committee consider succession planning for Board appointments;
- manage the business of the Board and set the agenda, style and tone of Board discussions to promote effective decision-making and constructive debate;
- facilitate the effective contribution and encourage active engagement by all members of the Board;
- in conjunction with the Chief Executive and Chief Governance Officer and Board Counsel, ensure that members of the Board receive accurate, timely and clear information to enable the Board to lead RBS, take sound decisions and monitor effectively the performance of executive management;
- ensure that the performance of individual directors and of the Board as a whole and its committees is evaluated regularly; and
- ensure RBS maintains effective communication with shareholders and other stakeholders.

Corporate governance

Chief Executive

The Chief Executive has responsibility for all of RBS's business and acts in accordance with the authority delegated by the Board.

The Chief Executive's key responsibilities are to:

- exercise executive accountability for the RBS businesses delivering operational management and oversee the full range of activities of the customer businesses and functions;
- develop, drive and deliver the strategy approved by the Board;
- drive and deliver performance against financial plans, acting in accordance with authority delegated by the Board;
- consult regularly with the Chairman and Board on matters which may have a material impact on RBS;
- act as champion of the culture and values of RBS, creating an environment where employees are engaged and committed to good customer outcomes;
- lead, manage and develop RBS's senior leadership team, ensuring professional capability is developed and that succession coverage meets the needs of RBS;
- ensure RBS has effective frameworks and structures to identify, assess and mitigate risks; and
- in conjunction with the Chairman and Chief Governance Officer and Board Counsel, ensure the Board receives accurate, timely and clear information.

Senior Independent Director

Sandy Crombie, as Senior Independent Director, acts as a sounding board for the Chairman and as an intermediary for other directors when necessary. He is also available to shareholders to discuss any concerns they may have, as appropriate.

Non-executive directors

Along with the Chairman and executive directors, the non-executive directors are responsible for ensuring the Board fulfils its responsibilities under its terms of reference. The non-executive directors combine broad business and commercial experience with independent and objective judgement and they provide independent challenge to the executive directors and the leadership team. The balance between non-executive and executive directors enables the Board to provide clear and effective leadership across RBS's business activities.

The standard terms and conditions of appointment of non-executive directors are available on rbs.com or from RBS Corporate Governance and Regulatory Affairs.

Board Committees

In order to provide effective oversight and leadership, the Board has established a number of Board committees with particular responsibilities. Please see page 54 of the Strategic Report for more details. The terms of reference are available on rbs.com.

The Board Committee established in 2015 in relation to the Financial Conduct Authority review of the treatment of SME customers continued to meet during 2016, to oversee and provide advice to the Board in relation to the review, the external independent review of Global Restructuring Group (GRG) instigated by the Group and other matters generally related to GRG. A new US Risk Committee was established to comply with US enhanced prudential standards and reports key matters discussed to the BRC. The first meeting took place in May 2016.

Chief Governance Officer and Board Counsel

Aileen Taylor is the Chief Governance Officer and Board Counsel and the Company Secretary. As of 1 January 2017, she also leads the bank's Regulatory Affairs function as part of an extended remit.

The Chief Governance Officer and Board Counsel's key responsibilities include:

- working closely with the Chairman to ensure effective functioning of the Board and appropriate alignment and information flows between the Board and its committees, including the Executive Committee. This includes Board succession planning, induction, and professional development;
- providing support and advice to the Board on a broad range of strategic, governance, legal and regulatory issues;
- executive responsibility for Chairman/non-executive director search and appointment process;
- management of the bank's profile with key stakeholders, including oversight of relations with key influencers, such as regulators;
- defining and delivering the corporate governance and regulatory affairs strategy across RBS; and
- the provision of professional support to the Board and its committees and leading on implementation of recommendations from the annual Board evaluation.

Conflicts of interests

RBS has procedures in place to ensure that the Board's management of conflicts of interest and its powers for authorising certain conflicts are operating effectively. On appointment, each director is provided with RBS's guidelines for referring conflicts of interest to the Board. Each director is required to notify the Board of any actual or potential situational or transactional conflicts of interest and to update the Board with any changes to the facts and circumstances surrounding such conflicts.

Situational conflicts can be authorised by the Board in accordance with the Companies Act 2006 and the company's Articles of Association. The Board considers each request for authorisation on a case by case basis and has the power to impose conditions or limitations on any authorisation granted as part of the process.

Details of all directors' conflicts of interest are recorded in a register which is maintained by the Chief Governance Officer and Board Counsel and reviewed annually by the Board.

Corporate governance

Board meetings

In 2016, nine Board meetings were scheduled and individual attendance by directors at these meetings is shown in the table below.

In addition to the nine scheduled meetings, 11 additional meetings and committees of the Board were held, including meetings to consider and approve financial statements. The Chairman and the non-executive directors meet at least once per year without executive directors present.

	Attended/ scheduled
Howard Davies	9/9
Ross McEwan	9/9
Ewen Stevenson	9/9
Sandy Crombie	9/9
Frank Dangeard (1)	5/5
Alison Davis	9/9
Morten Friis	9/9
Robert Gillespie	9/9
Penny Hughes	9/9
Brendan Nelson	9/9
Baroness Noakes	9/9
Mike Rogers (2)	9/9

Notes:

(1) Appointed to the Board on 16 May 2016.

(2) Appointed to the Board on 26 January 2016.

Principal areas of Board focus during 2016

In advance of each Board meeting, the directors are provided with comprehensive papers.

At each Board meeting the directors received reports from the Chairman, Chief Executive, Chief Financial Officer, Chief Risk Officer, Chief Conduct and Regulatory Affairs Officer, Franchise CEOs and the Board Committee Chairmen. An overview of the principal areas of Board focus during 2016 is set out below:

Customer

- customer service
- network distribution
- products and innovation
- branding
- culture
- customer trust and advocacy

Finance

- annual financial budget and plan
- capital strategy and planning
- Internal Capital Adequacy Assessment Process
- Individual Liquidity Adequacy Assessment
- pension funding
- recovery and resolution planning
- results and analysts' presentations

Strategy

- annual Board strategy offsite
- EU referendum implications
- Ring-fencing, including legal entity restructuring
- transactions updates
- transformation programme
- Williams & Glyn disposal
- technology updates

Risk & Conduct

- stress testing
- risk appetite governance and framework
- annual review of strategic risk appetite
- Individual Accountability Regime implementation

Legal & Governance

- Annual Report and Accounts
- AGM arrangements
- board appointments
- board and committee evaluation
- annual PRA and FCA presentation to the Board
- external auditor evaluation
- internal audit evaluation
- legal report, including litigation updates

Human Resources

- employee survey results
- executive director remuneration proposals
- executive talent session

During 2016 the Board also visited the Ulster Bank business in the Republic of Ireland, spending time on the business, risks and challenges. The directors met with key customers, politicians and senior industry and business representatives.

Executive Committee

Executive Committee members attend part of each Board meeting to provide an update on the performance of each of the franchises and risk, operational and conduct issues. Other relevant senior executives attend Board meetings to present reports to the Board as appropriate. This provides the Board with an opportunity to engage directly with management on key issues and supports the Board's succession planning activity.

Board effectiveness

Skills and experience of the Board

The Board is structured to ensure that the directors provide RBS with the appropriate balance of skills, experience and knowledge as well as independence. Given the nature of RBS's businesses, experience of banking and financial services is clearly of benefit, and we have a number of directors with substantial experience in that area. The Board also benefits from directors with experience in other fields.

Corporate governance

The table below illustrates the breadth of skills and experience on the Board.

• Retail Banking	• Chief Executive experience
• Broad Financial Services	• Finance & Accountancy
• Markets/Investment Banking	• Risk
• Government & Regulatory	• Technology/Digital
• Mergers & Acquisitions	• Operations
• Corporate Restructuring	• Change Management
• Stakeholder Management	• Consumer Facing

Board committees also comprise directors with a variety of skills and experience so that no undue reliance is placed on any individual.

Induction and professional development

Each new director receives a formal induction on joining the Board, which is co-ordinated by the Chief Governance Officer and Board Counsel. This includes visits to RBS's major businesses and functions and meetings with directors and senior management. Meetings with external auditors, counsel and stakeholders are also arranged as appropriate. An illustrative list of the meetings arranged during a new director's induction programme is set out below:

Chairman	Director, Finance
Chief Executive	Chief Accountant
Chief Financial Officer	Head of RBS Tax
Senior Independent Director	Chief Human Resources Officer
Other non-executive directors	Chief Administrative Officer
Chief Governance Officer and Board Counsel	Head of Investor Relations
Chief Risk Officer	Head of Public Affairs
Chief Marketing Officer	Director of Strategy & Corporate Development
Chief Operating Officer	Director of Transformation
RBS Treasurer	Head of Restructuring
Chief Audit Executive	Chief Economist
Chief Legal Officer and General Counsel	External Auditors
Chairmen and CEOs of principal subsidiaries	External Counsel
Franchise Chief Executive Officers	Regulators
	Institutional Investors
	Business visits (UK and overseas)

The directors have access to a wide range of briefing and training sessions and other professional development opportunities. Internal training relevant to the business of RBS is also provided. Business visits are arranged as part of the Group Audit Committee and Board Risk Committee schedule (details of which can be found on pages 73 and 80) and all non-executive directors are invited to attend. Directors undertake the training they consider necessary to assist them in carrying out their duties and responsibilities as directors. Directors may also request individual in-depth briefings from time to time on areas of particular interest.

During 2016, the directors received updates on a range of subjects to enhance their knowledge, including:

- investor and rating agencies views on RBS;
- disruptive technologies;
- Market Abuse Regulations (Inside Information and Persons Discharging Management Responsibility aspects);
- corporate investigations;
- Senior Managers' Regime;
- The Conduct Rules;
- PRA's final Supervisory Statement on corporate governance and board responsibilities;
- Ring-fencing;
- board diversity;
- The UK Government's proposals for corporate governance reform;
- Institute of Directors 2016 good governance report;
- FRC's report on corporate culture and the role of the board; and
- key regulatory & supervisory policy developments.

The Chief Governance Officer and Board Counsel maintains continuing professional development logs. These are reviewed regularly between the Chairman and each director individually, to assist in identifying future training and development opportunities that are specific to the individual director's requirements.

Information

All directors receive accurate, timely and clear information on all relevant matters and have access to the advice and services of the Chief Governance Officer and Board Counsel. In addition, all directors are able, if necessary, to obtain independent professional advice at the company's expense.

Time commitment

It is anticipated that non-executive directors will allocate sufficient time to RBS to discharge their responsibilities effectively and will devote such time as is necessary to fulfil their role. Directors have been briefed on the limits on the number of other directorships that they can hold under the requirements of the fourth Capital Requirements Directive (CRD IV). Each director is required to advise RBS as early as possible and to seek the agreement of the Board before accepting additional commitments that might affect the time the director is able to devote to his or her role as a non-executive director of RBS. The Board monitors the other commitments of the Chairman and directors and is satisfied that they are able to allocate sufficient time to enable them to discharge their duties and responsibilities effectively. The time commitment currently required of our non-executive directors continues to be significant.

Election and re-election of directors

In accordance with the provisions of the Code, all directors stand for election or re-election by shareholders at the company's Annual General Meeting. In accordance with the UK Listing Rules, the election or re-election of independent directors also requires approval by a majority of independent shareholders.

Corporate governance

Performance evaluation

In accordance with the Code, an external evaluation of the Board takes place every three years. An internal evaluation takes place in the intervening years.

The 2015 evaluation was conducted externally by a specialist board evaluation consultancy and a number of initiatives were implemented aimed at improving the overall performance and effectiveness of the Board. These included the creation of a Nominations and Governance Committee, adding a governance oversight function and streamlining processes and membership; a range of actions to enhance agenda planning and the Board's overall operating rhythm; and actions to improve alignment between the Board and executives to ensure a consistent "tone from the top". These themes were taken forward during 2016 under an action plan, are being appropriately addressed and will be kept under regular review as a matter of good practice.

In 2016, the Board and committee evaluation process was conducted internally by the Chief Governance Officer and Board Counsel.

Performance evaluation process

The Chief Governance Officer and Board Counsel undertook a formal and rigorous evaluation by:

- preparing surveys that were completed by each director and holding interviews with each director;
- discussing the key themes and recommendations for action with the Chairman; and
- recommending the key themes and proposed actions to the Board.

Outcomes of the 2016 performance evaluation

The 2016 performance evaluation concluded that the Board was strong and operated effectively and within its terms of reference.

Key strengths identified included the following:

- The Chairman provides strong leadership to the Board and has settled into the role well.
- The Board works well together to create effective debate and challenge, and provides effective oversight and challenge to management.
- The Board's composition has been strengthened during 2016 by the appointments of Mr Rogers and Mr Dangeard.
- The quality of information received by the Board continues to improve.
- The Board's committees operated effectively within their terms of reference throughout the year, providing valuable support to the Board.

A summary of the key themes arising from the 2016 performance evaluation is set out below, together with an overview of the key actions proposed:

Key themes

Board composition and succession planning

The importance of keeping Board and committee composition under regular review was highlighted, in order to ensure diversity and an orderly succession as a number of non-executive directors approach the end of their tenure with RBS.

Quality of information

Paper quality has improved over recent years. There is scope for further enhancement, by continuing to manage paper length and ensuring an appropriate level of detail is shared with the Board. Similar issues were raised during the committee evaluations.

Focus of agenda

The balance of the Board agenda tends towards legacy and internal issues, which reflects the current climate. However, it is also important to ensure continued focus on forward-looking and strategic discussions.

Non-executive director time commitment

Non-executive director time commitment remains significant. This is largely due to the number of extraordinary items which require to be considered by the Board in the current environment.

Customers and culture

The Sustainable Banking Committee has played a key role in customer and culture issues, however the directors would welcome greater Board focus on these priorities.

Proposed actions

Recommendations arising out of the 2016 evaluation have been carefully considered by the Board. An action plan has been agreed for 2017 and key actions include:

- Ensuring board & committee composition and succession plans are kept under regular review, to be led by the Group Nominations and Governance Committee.
- Refreshing Board and committee paper templates and guidance, to ensure consistency across the Board and committees in relation to paper length and content.
- Ensuring Board time is appropriately allocated in response to evaluation feedback, to facilitate the effective use of non-executive director time.
- Further developing the Board's role on culture, to include consideration of how Board time is spent on actions to drive cultural change.

In addition, a list of 2017 priorities for the Board was prepared following evaluation feedback and has been factored into the 2017 agenda planning process, as appropriate.

Individual director and Chairman effectiveness reviews

The Chairman met with each director individually to discuss their own performance and ongoing professional development and also shared peer feedback provided as part of the evaluation process. Separately, the Senior Independent Director sought feedback on the Chairman's performance from the non-executive directors, executive directors and key external stakeholders and discussed it with the Chairman.

Corporate governance

Relations with investors

The Chairman is responsible for ensuring effective communication with shareholders. The company communicates with shareholders through the Annual Report and Accounts and by providing information in advance of the Annual General Meeting. Individual shareholders can raise matters relating to their shareholdings and the business of RBS at any time throughout the year by letter, telephone or email via rbs.com/ir.

Shareholders are given the opportunity to ask questions at the Annual General Meeting and any General Meetings held or can submit written questions in advance. The Senior Independent Director and the chairmen of the Board committees are available to answer questions at the Annual General Meeting.

Communication with the company's largest institutional shareholders is undertaken as part of the Investor Relations programme:

- the Chief Executive and Chief Financial Officer meet regularly with UKFI, the organisation set up to manage the Government's investments in financial institutions, to discuss the strategy and financial performance of the business. The Chief Executive and Chief Financial Officer also undertake an extensive annual programme of meetings with the company's largest institutional shareholders;
- the Chairman independently meets with RBS's largest institutional shareholders annually to hear their feedback on management, strategy, business performance and corporate governance. Additionally, the Chairman, Senior Independent Director and chairmen of the Board committees met with the governance representatives of a number of institutional shareholders during the year;
- the Senior Independent Director is available if any shareholder has concerns that they feel are not being addressed through the normal channels; and
- the Chairman of the Group Performance and Remuneration Committee consults extensively with major shareholders in respect of the Group's remuneration policy.

Throughout the year, the Chairman, Chief Executive, Chief Financial Officer and Chairman of the Group Performance and Remuneration Committee communicate shareholder feedback to the Board. The directors also receive reports reviewing share price movements and performance against the sector. Detailed market and shareholder feedback is provided to the Board after major public announcements such as a results release. The arrangements in place are to ensure that directors develop an understanding of the views of major shareholders and that these are considered as part of the annual Board evaluation.

The Investor Relations programme also includes communications aimed specifically at its fixed income (debt) investors. The Chief Financial Officer and/or the RBS Treasurer give regular presentations to fixed income investors to discuss strategy and financial performance. There is also a separate section on the RBS website for fixed income investors which includes information on credit ratings, securitisation programmes and securities documentation. Further information is available at rbs.com/ir.

Report of the Group Nominations and Governance Committee

Letter from Howard Davies Chairman of the Group Nominations and Governance Committee



Dear Shareholder,

As Chairman of the Board and Chairman of the Group Nominations and Governance Committee I am pleased to present our report on the committee's activity during 2016.

Role and responsibilities

The Group Nominations and Governance Committee was constituted in January 2016 and assumed the responsibilities of the previous Group Nominations Committee to review the structure, size and composition of the Board, and membership and chairmanship of Board Committees. In addition, the Committee monitors the Group's governance arrangements to ensure that best corporate governance standards and practices are upheld and considers developments relating to banking reform and analogous issues affecting the Group in the markets where it operates. The Committee makes recommendations to the Board in respect of any consequential amendments to the Group's operating model.

The Committee engages with external consultants, considers potential candidates and recommends appointments of new directors to the Board.

The terms of reference of the Group Nominations and Governance Committee are reviewed annually, approved by the Board and are available at rbs.com.

Principal activity during 2016

As highlighted in the Board's 2015 performance review, the Committee acknowledges the tenure of a number of the current Board directors and therefore made succession planning a priority in 2016.

In addition to recruitment, the Committee assumed oversight of the process to reach agreement with the PRA in respect of a governance model that adheres to ring-fencing legislation. Ring-fencing also gives rise to a requirement to recruit additional non-executive directors to the boards of our material regulated subsidiaries, which the Committee has also been overseeing.

The Committee has spent time considering the Group's arrangements in respect of legal entity governance. This work is ongoing and is complementary to the Group's preparations for the implementation of ring-fencing legislation.

Membership and meetings

The Group Nominations and Governance Committee is comprised of the Chairman of the Board and four independent non-executive directors, which is consistent with the findings of last year's recommendation. The Committee holds at least four scheduled meetings per year and also meets on an ad hoc basis as required. In 2016, there were four Group Nominations and Governance Committee meetings and individual attendance by directors at these meetings is shown in the table below.

	Attended/ scheduled
Howard Davies (Chairman)	4/4
Sandy Crombie	4/4
Alison Davis	4/4
Robert Gillespie	4/4
Brendan Nelson	4/4

Consideration of new non-executive directors

As previously advised, JCA Group has been engaged to support the search for new non-executive directors. The search and nominations process has been streamlined, including by establishment of this Committee. The Committee has also considered (by reference to peer institutions) the significant time commitment required of the Group's non-executive directors and how this might be reduced to make the position accessible to a larger pool of candidates. JCA group does not provide search services to any other part of RBS.

During 2016, the Committee considered a number of potential candidates and in May 2016, Frank Dangeard was appointed to the Board as a non-executive director.

The Committee has overseen the establishment of the Group's Technology Advisory Board, which was constituted on 1 December 2016 with a remit to provide an external lens to RBS's innovation and technology agenda including consideration of driving a resilient, simple and efficient technology environment.

In addition to appointments to the Board (and subsidiary appointments being required to specifically comply with ring-fencing legislation), the Committee has also overseen the process for the appointment of a new chairman for Ulster Bank Ireland DAC.

Tenure of non-executive directors

The tenure of non-executive directors is set out below.

	2016
0 - 3 years	40%
3 - 6 years	30%
6 + years	30%
	<hr/> 100%

Report of the Group Nominations and Governance Committee

Board and Committee membership

As previously mentioned, Frank Dangeard joined the Board as a non-executive director on 16 May 2016 and was subsequently appointed to the Board Risk Committee on 4 August 2016. Frank has substantial Board level experience across a number of sectors, including technology, telecom and financial services. His change management and transformation experience are a real asset to the Board.

The Committee recommended in February 2016 that the CIB Board Oversight Committee should be discontinued, due to its remit having been superseded.

Performance evaluation

The annual review of the effectiveness of the Board and its senior Committees, including the Group Nominations and Governance Committee, was conducted internally in 2016. The Committee has considered and discussed the outcomes of this evaluation and accepts the findings. Overall the review concluded that the Group Nominations and Governance Committee operated effectively. However, certain recommendations for action were recognised including the need to: regularly engage with the external search firm to provide clarity and guidance on RBS's recruitment requirements; and rebalance the agenda of the Committee to ensure greater focus on strategic issues, including director performance and board and senior management succession.

The outcomes of the evaluation have been reported to the Board and the Committee will track progress during the year.

Boardroom diversity

The Board currently meets the target of 25 per cent female board representation as set out in Lord Davies' 2011 report on women on Boards. We acknowledge the updated targets published in the Hampton Alexander and Parker reports and will continue to consider the implications for RBS during 2017.

The gender diversity of the Board is set out below.

	2016
Female	25%
Male	75%
	<hr/> 100%

The Board operates a boardroom diversity policy and a copy of the Board's diversity statement is available on [rbs.com>about us](http://rbs.com/about-us).

RBS understands the importance of diversity and, with regard to gender diversity, recognises the importance of women having greater representation at key decision making points in organisations. The search for Board candidates will continue to be conducted, and nominations/appointments made, with due regard to the benefits of diversity on the Board. However, all appointments to the Board are ultimately based on merit, measured against objective criteria, and the skills and experience the individual can bring to the Board.

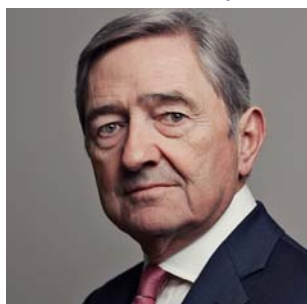
The balance of skills, experience, independence, knowledge and diversity on the Board, and how the Board operates together as a unit is reviewed annually as part of the Board evaluation. Where appropriate, findings from the evaluation will be considered in the search, nomination and appointment process. If appropriate, additional targets on diversity will be developed in due course.

Further details on RBS's approach to diversity can be found on pages 118 and 119.

Howard Davies
Chairman of the Group Nominations and Governance Committee
23 February 2017

Report of the Group Audit Committee

**Letter from Brendan Nelson,
Chairman of the Group Audit Committee**



“The first priority of the Group Audit Committee is to ensure the integrity and quality of RBS’s financial statements”

Dear Shareholder,

Throughout 2016 RBS has continued to progress its plan to build a strong, simple, fair bank for customers and shareholders and the Group Audit Committee (GAC) has supported this through the review and consideration of RBS’s financial reports and disclosures. This report also sets out the key areas of focus for the GAC during 2016. I am pleased to confirm that the GAC operated effectively during 2016, as was confirmed by the annual evaluation process, details of which are also set out below.

Accounting and financial reporting

The first priority of the GAC is to ensure the integrity and quality of RBS’s financial statements, including its quarterly, interim and full year results and its annual report and accounts. During 2016 the GAC spent considerable time reviewing and discussing RBS’s financial results in detail, and challenging the material judgements proposed by management, before recommending them to the Board for approval.

In particular, during 2016 the GAC considered judgements relating to the recoverability of deferred tax assets, the carrying value of goodwill, provisions for litigation and conduct charges, loan impairment provisions and the fair value of financial instruments. Additionally, in the stand-alone parent company accounts, the GAC considered judgements relating to the carrying value of RBSG’s investment in subsidiaries.

There were also a number of developments during 2016 which required the GAC’s scrutiny from a disclosure perspective. The divestment of Williams & Glyn was an important issue during 2016 and the GAC was fully engaged on this issue in order to ensure that all developments and risks were transparently disclosed to the market. RBS also continues to work through a number of litigation and conduct issues which the GAC has carefully considered in order to ensure its disclosures remain accurate and up to date.

The implications of the EU referendum and subsequent developments in the macro economic environment were an important area of focus for RBS in the second half of 2016. The GAC received reports on the implications for the credit environment which it has considered in the context of RBS’s disclosures and financial reports. This will remain an area of ongoing focus into 2017.

The Market Abuse Regulation took effect in July 2016. The GAC reviewed and discussed the implications for RBS’s disclosures and the processes RBS has implemented to ensure compliance with these regulations.

The GAC also considered significant developments in relation to financial reporting to ensure that RBS is well prepared for legal and regulatory changes which impact its financial results and disclosures. In particular, the GAC has overseen the preparatory work relating to the introduction of IFRS 9 which will take effect on 1 January 2018.

In relation to the Annual Report and Accounts, the GAC carefully considered the viability report and the ‘fair, balanced and understandable’ statement, including the processes which support them. The directors are required to make these statements in line with the UK Corporate Governance Code.

Systems of internal control

RBS continues to work on the improvement of its control environment, which is key to making RBS a safer and more secure bank. However, the level of change RBS is undergoing presents significant challenges and RBS’s operational risk profile remains heightened. The GAC oversees the arrangements for RBS’s systems of Internal Control relating to financial reporting. During 2016 the GAC received quarterly updates from Internal Audit detailing Internal Audit’s control ratings for RBS’s businesses and functions. The GAC also received bi-annual updates on the control environment certification process and the material operational risk events which are notified to RBS’s senior management, executives and non-executive directors.

During 2016 RBS made good progress in developing its operational risk management framework with the roll-out of bank-wide risk appetite statements for its most material risks, this included financial reporting risk appetite which was considered by the GAC in August 2016. RBS has also developed end to end risk and control assessment for material processes during 2016, and the resulting actions to improve and enhance controls will be taken forward during 2017; this process will be overseen by the Board Risk Committee with the GAC focusing on those aspects impacting financial reporting. The drive to achieve satisfactory controls will benefit from the bank-wide programme to enhance risk culture, with its focus on encouraging a proactive approach to risk and a more open and challenging environment.

External audit

A priority for the GAC during 2016 was to oversee a change of the external auditors. Ernst & Young (EY) assumed the role of RBS’s new auditors in March 2016, having been successful in the tender process run in 2014.

On behalf of the GAC, I would like to thank the outgoing external auditors, Deloitte LLP, for their hard work over many years and for their professionalism in ensuring an orderly and smooth handover to EY.

The external auditors have attended each meeting of the GAC in 2016 and have provided the GAC with quarterly reports and ad hoc updates on specific topics as required. I am pleased to confirm that the 2016 evaluation of the external auditor found that EY were performing the audit of RBS effectively.

Report of the Group Audit Committee

Key priorities for 2017

Moving into 2017 the GAC will continue its focus on RBS's accounting and financial reporting. The GAC will continue to consider developments in accounting policy and regulations impacting RBS, including IFRS 9 in particular. The impact of developments in the macro economic environment on the credit portfolio and financial results will also remain a priority, as will the Control Environment and the GAC will continue to monitor these throughout 2017.

Accounting issues and disclosures relating to legacy litigation and conduct issues are also expected to be an important area of attention during 2017 as had been demonstrated by the provision RBS announced on 26 January 2017 in relation to RMBS litigation and investigations.

I would like to take this opportunity to thank my fellow GAC members for their continued support and focus during 2016.

Brendan Nelson
Chairman of the Group Audit Committee
23 February 2017

Report of the Group Audit Committee

Report of the Group Audit Committee

Membership

The Group Audit Committee (GAC) is comprised of the following four independent non-executive directors.

	Attended/ scheduled
Brendan Nelson (Chairman)	7/7
Sandy Crombie	7/7
Morten Friis	7/7
Baroness Noakes	7/7

Brendan Nelson, Morten Friis and Baroness Noakes are also members of the Board Risk Committee. Sandy Crombie is Chairman of the Group Performance and Remuneration Committee. Brendan Nelson and Sandy Crombie are also members of the Group Nominations and Governance Committee. This cross committee membership helps facilitate effective governance across all finance, risk and compensation issues. It also helps to ensure that agendas are aligned and that overlap of responsibilities is avoided where possible.

The members of GAC are selected with a view to the expertise and experience of the GAC as a whole and with proper regard for the key issues and challenges facing RBS.

The Board is satisfied that all GAC members have recent and relevant financial experience and that each member of the GAC is independent as defined in the SEC rules under the US Securities Exchange Act of 1934 (the "Exchange Act") and related guidance. The Board has further determined that Brendan Nelson, Committee Chairman, and Baroness Noakes are both 'financial experts' for the purposes of compliance with the Exchange Act Rules and the requirements of the New York Stock Exchange, and that they have competence in accounting and auditing as required under the Disclosure Guidance and Transparency Rules. Full biographical details of GAC members are set out on pages 59 to 61.

During 2016 GAC meetings were attended by the Chief Executive and Chief Financial Officer; the Group Chairman; the Internal and External Auditors; and Finance, Legal and Risk Management executives. Other executives, subject matter experts and external advisers were also invited to attend, as required, to present and advise on reports commissioned by the GAC. The GAC also met privately with the external auditors and separately with Internal Audit management.

Purpose of the Group Audit Committee

The GAC's responsibilities are set out in more detail in its terms of reference which are reviewed annually by the Committee and approved by the Board. These are available on: rbs.com.

Meetings and visits

The GAC held seven scheduled meetings during 2016, four of which were held immediately prior to the submission of the quarterly financial statements to the Board. The GAC also convened three ad hoc meetings to consider:

- the trading statement issued in January 2016;
- documentation relating to disclosures in the 2015 Annual Report and Accounts; and
- disclosure issues relating to the H1 2016 results, including the developments on Payment Protection Insurance.

During 2016, in conjunction with members of the Board Risk Committee, members of the GAC took part in an annual programme of visits to businesses and control functions in order to gain a deeper understanding of the risks and issues they face. This programme comprised two visits to Risk and Restructuring; Conduct and Regulatory Affairs and Internal Audit plus visits to: Personal & Business Banking; Commercial & Private Banking; NatWest Markets (formerly CIB); Capital Resolution, Services; and Finance.

Allocation of Group Audit Committee agenda time during 2016 was as follows:

Financial affairs of the group	39%
Standards of internal control	21%
Internal audit	13%
External audit	9%
Regulatory relationships and compliance	13%
Governance and procedural	5%
Total	100%

Performance evaluation

The performance of the GAC is evaluated annually, and at least once every three years is facilitated by an external party. Following an externally facilitated evaluation in 2015, the evaluation of the GAC's performance in 2016 was conducted internally. The evaluation process involved the completion of questionnaires by both GAC members and members of management and follow up interviews to discuss the findings. The Board and the GAC have considered and discussed the outcomes of this evaluation. Overall the review concluded that the GAC continued to operate effectively. A number of recommendations for improvement were made which were approved by the GAC and the Board; progress against these will be tracked in 2017.

Report of the Group Audit Committee

Matters considered by the Committee in 2016

Key area	Matters considered and action taken by the Committee
Financial affairs of the Group	
Accounting judgements and reporting issues considered in the preparation of financial reports	<p>The Group Audit Committee focused on a number of salient judgements and reporting issues in the preparation of the financial results throughout 2016, including the quarterly, half year and full year results and the Annual Report and Accounts. In particular, the Committee considered, discussed and, where appropriate, challenged:</p> <ul style="list-style-type: none"> • provision and disclosure for ongoing regulatory and litigation actions including: Payment Protection Insurance claims, RMBS investigations and litigation, UK shareholder actions, the FCA's investigation into RBS's former Global Restructuring Group, the Central Bank of Ireland's review of Irish tracker mortgages and investigations into alleged foreign exchange rate manipulation. During 2016 RBS has recognised £5.9 billion of litigation and conduct provisions; • the adequacy of loan impairment provisions, focusing in particular on judgements and methodology applied to provisions. The Committee was satisfied that the overall loan impairment provisions and underlying assumptions and methodologies were reasonable and applied consistently; • valuation methodologies and assumptions for financial instruments carried at fair value including RBS's credit market exposures and own liabilities assessed at fair value; • judgements made by management in relation to the carrying value of intangible assets. In particular, in light of changes to economic forecasts, the GAC considered whether any adjustments were required to the carrying value of goodwill and of RBS's investment in subsidiaries within the stand-alone parent company accounts; in its Q3 2016 results RBSG reduced the carrying value of its investment in subsidiaries by £6.0 billion to £44.7 billion in light of the deterioration in the economic outlook. The GAC also challenged the processes and the models used to assess the value of these assets; • judgements made by management in assessing the recoverability of deferred tax assets, in light of continued execution of the RBS's strategy and changes to the UK corporate tax system. A £300 million impairment of deferred tax assets was recognised in RBS's Q3 2016 results; • management's assessment of the adequacy of internal controls over financial reporting, and identified deficiencies. Remediation of identified weaknesses in relation to privileged access controls for certain IT applications and in relation to legal entity recharge accounting for the allocation of ATM fees was monitored and tracked by the GAC during 2016; • the quality and transparency of financial and risk disclosures; • the viability statement in the 2016 report and accounts. The GAC considered the process to support the assessment of principal risks; assessed the company's prospects in the light of its current position and the identified principal risks; selected the time period to be covered by the statement; and reviewed the disclosure on behalf of the Board; • the going concern basis of accounting including consideration of evidence of RBS's capital, liquidity and funding position. The GAC supported the directors' going concern conclusion. Further information is set out on page 119; and • the comprehensive review process which supports the GAC and the Board in reaching the conclusion that the disclosures in the Annual Report and Accounts, taken as a whole, are fair, balanced and understandable and provided the information necessary for shareholders to assess the company's position and performance, business model and strategy. The review process included: central co-ordination of the annual report and accounts by the Director of Finance with guidance on requirements being provided to individual contributors; review of the annual report and accounts by the Executive Disclosure Committee prior to consideration by the GAC; and a management certification process which required members of the Executive Committee and other senior executives to provide confirmation following their review of the annual report and accounts that they considered them to be fair, balanced and understandable. This process was also undertaken in respect of the half year and quarterly results announcements. The External Auditor also considered the Board's statement as part of its audit requirements. <p>Having considered the above, the Committee recommended the quarterly, interim and full year results announcements and the Annual Report and Accounts to the Board for approval.</p>

Report of the Group Audit Committee

Key area	Matters considered and action taken by the Committee
Standards of internal control	
Annual Risk and Control report	The GAC considered the effectiveness of RBS's internal control system, including any significant failings or weaknesses. The Williams & Glyn divestment programme and the NatWest Markets control environment were both identified as weaknesses, these have both been closely monitored and reviewed by the Board Risk Committee and are discussed further in the report of the Board Risk Committee. The GAC also considered RBS's disclosure on internal control matters in conjunction with the related guidance from the Financial Reporting Council.
Control Environment Certification	The GAC considered the outputs of bi-annual self-assessments of the robustness of the internal control environment for RBS's customer-facing businesses, and its support and control functions. This informs the control environment disclosure in the annual report and accounts.
Integrated Risk Assessment Approach	The GAC reviewed work undertaken on the bank's integrated risk assessment approach which is designed to provide a single approach to the assessment of risk mind sets and behaviours and risk capabilities, leading to a more effective and simplified approach to the assessment of risk culture, the three lines of defence and performance assessments.
Whistleblowing	The GAC received updates on whistleblowing activity and the performance of RBS's whistleblowing service. It monitored the effectiveness of the whistleblowing framework and enquired as to any trends or themes. It also received updates on communications and awareness activity relating to whistleblowing and testing of the framework. The GAC was also advised of the actions RBS has taken to ensure compliance with the new FCA and PRA whistleblowing regulations which applied to RBS from 7 September 2016. In March 2016 the GAC Chairman was appointed as Whistleblowing Champion for RBS, in line with the requirements outlined in the PRA and FCA regulations; this role carries the responsibility for ensuring and overseeing the integrity, independence and effectiveness of the firm's whistleblowing arrangements.
Ledger Transformation Programme	The GAC received updates in relation to the delivery of the new general ledger, the introduction of which has been overseen by the GAC. The new ledger replaces previous legacy systems and supports new functionality such as discrete legal entity views and multi-currency accounting on a single ledger platform. The GAC was provided with updates on the recommended actions and plans to deliver the programme and the key risks and challenges it presented.
Taxation	The GAC reviewed RBS's tax position, including a deep dive on Tax in October 2016 which covered; the structure of the Tax team, Tax Risk within the Risk Management Framework, material tax risks and disputes, UK Corporate tax compliance, deferred tax assets, VAT risks and challenges, external tax developments and the key projects on which the tax team are engaged.
Litigation and Regulation	The GAC considered regular reports on most significant legal risks and developments affecting RBS, including relevant updates on ongoing major litigation and investigations, privacy and competition issues, legal risks within structural reform and recovery and resolution planning, as well as material emerging legal risks and/or changes in law or regulation and any recent provisions and settlements or recoveries. Key themes and observations from RBS's Sensitive Investigations Unit were also highlighted to the GAC.
Notifiable Event Process	The GAC received bi-annual reports on control breaches which are captured by RBS's notifiable event process. Process-related errors were the main root cause of Major notifiable events escalated in 2016. Throughout 2016 senior management has actively promoted an open culture around raising GNEPs and regularly reinforced that these are integral in helping the bank's employees learn from their mistakes. Under this process all Board directors were alerted to the most significant breaches.
Fraud	The GAC reviewed management's processes for identifying and responding to the risk of fraud.
Sarbanes-Oxley Act of 2002	The GAC considered RBS's compliance with the requirements of the Sarbanes-Oxley Act of 2002, and was satisfied in this respect. RBS had no Material Weaknesses as at 31 December 2016, however Significant Deficiencies were identified relating to legal entity recharge arrangements and action is being taken by Management to improve these processes. The GAC has also overseen RBS's drive to continue to improve its SOX processes.

Report of the Group Audit Committee

Key area	Matters considered and action taken by the Committee
Systems of internal control	
Market Abuse Regulation	The GAC considered the impact of the Market Abuse Regulation which took effect in July 2016. The GAC noted the main changes to disclosure requirements and the processes implemented by RBS to address these. This included the establishment of a sub-committee of the executive disclosure committee to consider potential instances of inside information, including whether there are any grounds for delaying disclosure under the Market Abuse Regulation, and escalate these as required to the GAC and Board.
Internal audit	
Reports and Opinions	The GAC received quarterly reports and opinions from Internal Audit throughout 2016. These reports and opinions updated the GAC on the effectiveness of the governance, risk management and internal control framework, ongoing issues and the adequacy of remediation activity. The full year and half year reports included Internal Audit's opinion in relation to RBS's Risk & Control Environment and its Risk & Control Awareness. Internal Audit are now using the new simplified bank-wide risk and control rating metrics, which came into effect on 1 January 2016. The new metrics align the way RBS assesses its risks and controls across the first, second and third lines of defence. The GAC received updates on management's response to Internal Audit's findings and challenged management as to progress on remediating such findings.
Annual Plan and Budget	The GAC considered and approved Internal Audit's plan for 2017, which is focused on the highest risks faced by RBS. The GAC also considered Internal Audit's budget and was satisfied that this was sufficient to allow Internal Audit to deliver the plan.
Internal Audit Charter	Updates to Internal Audit's charter, to reflect changes in reporting structures and amendments to the Institute of Internal Auditors International Standards, were approved by the GAC and the GAC confirmed the independence of Internal Audit.
Visits	During two visits to Internal Audit in 2016, the GAC received updates on a variety of issues impacting the internal audit function, including; resourcing, bench strength, risk mindset and behaviours, strategic priorities, use of data analytics and internal quality assurance.
Chief Audit Executive	The Chief Audit Executive continued to report to the Chairman of the GAC, with a secondary reporting line to the Chief Executive for administrative purposes. The GAC assessed the annual performance (including risk performance) of the Chief Audit Executive.
Annual Evaluation	The annual review of effectiveness of Internal Audit was undertaken internally in 2016. Under the evaluation process feedback on Internal Audit was provided by GAC members and attendees (including the external auditors), chairmen of subsidiary audit committees, key members of business risk committees and other key members of management. The evaluation concluded that Internal Audit had operated effectively during the year. Certain recommendations were made to aid continuous improvement within the function; these will be implemented during 2017 and progress will be tracked by the GAC.
Relationship with regulators	
Regulatory Relationships, Risk of Enforcement and Upstream Risk	The GAC received a report on the status of RBS's relationships with its key regulators, the status of regulatory reviews, including any reviews at risk of potential enforcement action in 2016, and key upstream risk developments. The GAC Chairman also attended continuous assessment meetings with the PRA and FCA, meetings with the Bank of England and other audit committee chairmen and trilateral meetings with the PRA and external auditor.
External audit	
Transition of auditors	The GAC supervised the transition of the external auditor from Deloitte to EY during 2016 with EY assuming the role of external auditor for RBS at the end of March 2016. The Board will recommend the appointment of EY as external auditor to shareholders for approval at the Annual General Meeting.
External Audit Reports	Jon Bourne has been EY's lead audit partner for RBS since EY assumed the role of external auditor in March 2016. Jon Bourne attends each meeting of the GAC and reports to the GAC on the external auditor's observations and conclusions from the year-end audit and half-year review of The Royal Bank of Scotland Group plc, The Royal Bank of Scotland plc and National Westminster Bank Plc, work in connection with the Q1 and Q3 financial results and any recommendations for enhancements to RBS's reporting and controls.
Audit Plan and fees	The GAC received updates in relation to the external auditor's 2016 plan and approved the 2016 audit fees including the fee for the 2016 interim results. The GAC was authorised by shareholders at the Annual General Meeting to fix the remuneration of the external auditors.

Report of the Group Audit Committee

Key area	Matters considered and action taken by the Committee
External audit	
Annual Evaluation	The GAC conducted an internal evaluation to assess the independence and objectivity of the external auditor during 2016. This review included an evaluation of the effectiveness of the audit process and sought the views of the GAC members, attendees and other key members of management. Regard was had to the external auditor's mindset and culture, skills, character and knowledge, quality control and judgement. The evaluation concluded that the external auditor was operating effectively. A number of recommendations for continuous improvement were identified which the external auditor has agreed to take forward during 2017. Following the evaluation the GAC recommended that the Board seek the reappointment of EY as external auditor at the next annual general meeting.
CASS Opinions	At the GAC's request the external auditor presented the results of its assurance procedures on compliance with the FCA's Client Asset Rules for RBS's regulated legal entities for the year ended 31 December 2015. The GAC also considered the CASS Audit plan for 2017, the findings of which will be reported to the GAC once the audit is complete.
External Audit Report to the PRA	The GAC considered the 'dry run' report to the PRA by the external auditor for the 2015 year end. The report responded to specific questions posed by the PRA. This report was produced in preparation for implementation of auditor reporting for the largest UK banks which is required for 2016 year ends, in line with the proposals set out in PRA consultation paper CP8/15.
Audit and non-audit services	
Non-audit services policy	<p>To help safeguard the objectivity and independence of the external auditor, the GAC maintains a policy that sets out the circumstances in which the external auditor is permitted to supply audit and non-audit services. EY were appointed RBS's external auditors in March 2016 but they have been subject to the policy since becoming independent from RBS in 2015 in the lead up to their appointment.</p> <p>The GAC reviews the non-audit services policy at least annually to ensure it remains fit for purpose. During 2016 the GAC approved a number of amendments to the policy to ensure it met the requirements of the EU Audit Regulation and also to streamline to operation of the policy.</p> <p>In accordance with the policy, all audit services and permitted non-audit services are approved in advance.</p> <p>Under the policy certain services are classed as Audit-Related Services and these may be approved by the Director of Finance, on behalf of the GAC, up to a limit of £100,000 each financial quarter. Engagements for Audit-Related Services in excess of this quarterly limit require the approval of the GAC Chairman. All Audit-Related Services are reported to the GAC quarterly.</p> <p>The GAC has also delegated authority to the Director of Finance to approve the provision of services by the external auditor to non-consolidated subsidiaries of RBS within an annual cap and to approve engagements with the external auditor where RBS has limited or no influence in the selection process. All such engagements are reported to the GAC each quarter.</p> <p>For all other permitted non-audit service engagements, where the fee is below £5,000 approval by the Director of Finance is required. Where the fee is above £5,000 but below £100,000 approval by the GAC Chairman is required. For engagements where the fee is expected to exceed £100,000 a competitive tender process must be held and approval of the full GAC is required. In addition all engagements must be approved by the Director of Finance and by Supply Chain Services. All such ad hoc approvals of non-audit services are ratified by the GAC each quarter.</p>

Report of the Group Audit Committee

Key area	Matters considered and action taken by the Committee
Audit and non-audit services	
Non-audit Services Policy	<p>During 2016, the current and previous external auditors were approved to undertake the significant engagements set out below whilst in the role of external auditor:</p> <ul style="list-style-type: none"> • Deloitte were engaged to prepare an audit opinion, required by the PRA confirming the level of asset run down in RBS Capital Resolution, taking into accounting outstanding liabilities/indemnities to any disposed asset; details of any residual assets and how these will be managed following the closure of RBS Capital Resolution; and details of any ongoing obligations RBS will have to any disposed assets; • Deloitte's role as Reporting Accountant for Williams & Glyn was extended, to permit them to prepare a financial 'fact pack' to support the trade sale marketing of Williams & Glyn; • Deloitte were engaged to support Williams & Glyn with validation, review, quality assurance and documentation activities in relation to Williams and Glyn's capital stress plan; • Deloitte were engaged to support the first phase of a Central Bank of Ireland mandated investigation into tracker mortgages in Ulster Bank Rol. This first phase comprised the development and submission of a detailed plan for conducting the investigation and ensuring that appropriate governance was in place; • EY were engaged to review historical and prospective financial information for certain parts of the business; • EY were engaged to provide an assurance opinion for an information request from the European Commission in connections with its competition investigation into pre-2012 FX currency trading; and • EY were engaged to audit the control environment and control objectives for RBS and Ulster Bank's internal reporting procedures relating to the Scottish & Northern Ireland Banknote Rules 2011 and the Note Circulation Scheme Rules, as required by the Bank of England. <p>The decision to approve the engagement of the external auditor for the services noted above was due to factors including synergies and efficiencies relating to the audit work, their existing knowledge of RBS which allowed work to commence quickly and with minimal disruption and the benefits in maintaining consistency between similar engagements. In each case the GAC was satisfied that the engagement did not impact the external auditor's independence.</p> <p>Although RBS's previous external auditors are no longer subject to independence requirements, they do have an ongoing role to consent to the release of its prior period audit opinions for US reporting purposes (statutory and comfort letter related). Given any requirement to perform additional audit work for historic periods would require previous external auditors to re-establish independence, a number of safeguards relating to their appointment remain in place under the policy, including the requirement for engagements with Deloitte to be approved by the GAC or on its behalf by the Director of Finance (depending on the value of the engagement. Since Deloitte have been removed from independence requirements with these safeguards in place they have been engaged as follows:</p> <ul style="list-style-type: none"> • to provide additional quality assurance over management's assessment of the adequacy of SOX 404 control design and management's testing of the effective operation of SOX 404 controls; • as the skilled person to support the Bank's ring-fencing programme; • in relation to the remediation of the tracker mortgage book in Ulster Bank; • to provide resource support to help technology teams to implement and embed a new Technology delivery framework and; • to support the second phase of the Central Bank of Ireland mandated investigation into tracker mortgages in Ulster Bank. This second phase of work involves a review of Ulster Bank Ireland DAC's 2001-2015 mortgage loan book in line with the Central Bank of Ireland 'Framework for Conducting the Tracker Mortgage Examination'. <p>Further details of the non-audit services that are prohibited and permitted under the policy can be found on rbs.com. Information on fees paid in respect of audit and non-audit services carried out by the external auditor can be found in Note 5 on the consolidated accounts on page 325.</p>

Brendan Nelson
Chairman of the Group Audit Committee

Report of the Board Risk Committee

**Letter from Baroness Noakes
Chairman of the Board Risk Committee**



“RBS as a whole is on a journey towards a robust, well managed control environment”

Dear Shareholder,

The Committee had a challenging programme of risk issues to consider in 2016 and the report that follows provides details of the topics reviewed and debated by the Committee during the year. The Committee reviewed and provided oversight of the risk profile of the bank relative to the bank's strategy and risk appetite against the backdrop of an economic environment which is challenging for the bank and which was made more uncertain following the outcome of the EU referendum.

Strategic Risk and Transformation

The Committee continued to devote considerable attention to the demanding bank-wide transformation programme in 2016. In particular, it considered execution and delivery risk on behalf of the Board and monitored the amount of change risk faced by the business. We focused on the impact of transformation plans on the bank's control environment and on the control transformation workstream which is a key part of the overall programme. End to end risk and control assessments for material processes were carried out during 2016 and in 2017 we will be overseeing the improvement actions which are needed. The broader cost and control objectives of the transformation programme will continue to be a key priority in 2017 and future years.

Delivery of the Williams & Glyn separation programme remained a significant area of focus of the Committee in the first half of the year. In light of the delivery challenges, the Board decided to change its strategic direction and the committee subsequently focused on the wind-down of the programme.

As the year progressed, increasing agenda time was devoted to the implementation of the bank's ring-fencing programme as the programme moved from the design phase into the execution phase. The Committee reviewed the revised baseline plan before submission to the regulator and oversaw the development of an integrated assurance programme for the project involving Risk, Internal Audit and external third party assurance.

Control Environment

RBS as a whole is on a journey towards a robust, well-managed control environment and the Committee reviews the control ratings of significant business areas twice a year. Challenges are greatest within the bank's NatWest Markets (formerly CIB) franchise and we reviewed management's plans to strengthen substantively its control environment and address known weaknesses. We will oversee the effective delivery of those plans, relying in particular on more detailed challenge in the second line of defence.

Risk Appetite

The bank's risk appetite framework provides a structured approach to risk taking and the committee reviewed proposed enhancements to the framework prior to Board approval. We have extended our detailed examination beyond the suite of strategic risks to all material risk categories via a series of in depth reviews of the individual risk appetite statements and related metrics. These sessions enabled essential preparatory work to be undertaken prior to transitioning to a Board approval framework for these material risks in 2017. We will continue to supervise closely the maturing risk appetite framework, including remediation where breaches of material risk appetite are identified, in the year ahead.

Stress Testing

The bank conducted a number of stress tests in 2016 including the European Banking Authority and Bank of England stress tests in addition to its own internal stress tests. The Committee played a vital role in reviewing the scenarios and assumptions deployed and in ensuring that the outputs of the tests were subjected to a high degree of scrutiny and challenge. The Committee also oversaw enhancements to the bank's stress testing capability and this will remain a priority in 2017.

Other

Other material areas of Committee focus during the year have included:

- conduct risk and the oversight of on-going regulatory investigations and remediation;
- the capital and liquidity position of RBS and related regulatory submissions;
- cyber security including the outcome of RBS's participation in a cyber testing initiative led by the Bank of England (CBEST);
- risk culture, the three lines of defence model and risk performance assessments, now being combined into an integrated risk assessment process; and
- continued refinements to risk reporting.

Key priorities for 2017

The bank has made significant advances this year towards its goal of becoming a stronger, simpler and fairer bank. However, while progress has been made, more work is required before the bank will be operating fully within risk appetite and the Committee will keep this under review in 2017. In the coming year the Committee will also continue to oversee the work being carried out under the bank's significant change programmes and the impact of those initiatives on the risk profile of the bank. Other areas of focus of the Committee will include cyber risk, IT resilience and assessing the impact of external factors on the bank's risk profile.

I would like to conclude by welcoming Frank Dangeard to the Committee and by thanking my fellow Committee members for their continued support and diligence throughout the year. I would also like to extend my gratitude to Robert Gillespie, who stood down as a member in August, for his valuable contribution.

Baroness Noakes
Chairman of the Board Risk Committee
23 February 2017

Report of the Board Risk Committee

Report of the Board Risk Committee

The role and responsibilities of the Board Risk Committee

The Board Risk Committee (BRC) assumes responsibility on behalf of the Board to provide oversight of current and potential risk exposures and future risk strategy, including the determination of risk appetite and tolerance, and to promote a culture of risk awareness within RBS.

The BRC's responsibilities are set out in more detail in its terms of reference which are reviewed annually by the BRC and approved by the Board. These are available on RBS's website: rbs.com.

Membership

The Board Risk Committee comprises independent non-executive directors. Details of the skills and experience of each of the BRC members are set out in their biographies on pages 59 to 61.

	Attended/ scheduled
Baroness Noakes (Chairman)	9/9
Frank Dageard (1)	3/3
Morten Friis	9/9
Penny Hughes	9/9
Brendan Nelson	9/9
<hr/>	
Former Members	
Robert Gillespie(2)	6/6

Notes:

(1) Appointed to the committee on 4 August 2016.

(2) Stood down from the committee on 4 August 2016.

Brendan Nelson is chairman of the Group Audit Committee of which Baroness Noakes and Morten Friis are also members.

Penny Hughes is chairman of the Sustainable Banking Committee. This common membership across Committees helps to ensure effective governance across the committees.

BRC meetings are also attended by the RBS Chairman, relevant executives, including the Chief Executive, Chief Financial Officer, Chief Risk Officer, Chief Conduct & Regulatory Affairs Officer, Chief Legal Officer and General Counsel and Chief Audit Executive, and the lead partner of the External Auditor. External advice is sought by the BRC, where appropriate.

Meetings and visits

Nine scheduled meetings and six ad hoc meetings were held in 2016. The ad hoc meetings were required to consider: the results of various phases of internal and external stress tests; the Ring-Fencing Revised Baseline Plan; and the draft budgets and related stress test outputs.

In 2016, members of the BRC, in conjunction with members of the Group Audit Committee, undertook a programme of visits to focus on various businesses and control functions including bi-annual visits to Risk and C&RA. The purpose and scope of this programme is discussed in detail in the Report of the Group Audit Committee above.

The BRC also held in-depth sessions on risk reporting and the legal entity framework and associated capital requirements.

Performance Evaluation

The annual review of the effectiveness of the Board and its senior Committees, including the Board Risk Committee, was conducted internally in 2016. The BRC has considered and discussed the outcomes of this evaluation and accepts the findings. Overall the review concluded that the Board Risk Committee continued to operate effectively. However, certain recommendations for action were recognised including the need to: rebalance the agenda of the BRC to ensure sufficient focus on the most pertinent risks and reduce the length of meetings; place more reliance on executive committees to reduce pressure on the BRC' agenda; and hold Executives to account for sign-posting key issues and escalating a unified position from all three lines of defence.

The review included a small number of general recommendations which are relevant for both the Board and its senior committees. Key themes and actions arising from these general recommendations are set out in the Board report on page 67 and will be considered, and addressed as appropriate, at Board level.

The outcomes of the evaluation have been reported to the Board and the BRC will track progress on its 2017 priorities during the year.

Allocation of Board Risk Committee agenda time:

Current risk profile and issues	26%
Change agenda and large projects	10%
Process, policies and risk appetite	15%
Regulatory returns and stress testing	15%
Accountability and remuneration	6%
Risk, conduct and regulatory affairs focus sessions	13%
Franchise and function focus sessions	15%
Total	100%

Report of the Board Risk Committee

Matters considered by the Committee in 2016

Key area	Issues considered and Action taken by the BRC
Risk Profile	
Reporting	<ul style="list-style-type: none"> • Provided oversight of RBS's risk profile relative to RBS's strategy and risk appetite through the review of emerging risks and changes in RBS's most significant portfolios and operations, as presented within the comprehensive Risk Management Report. In order to focus on changes in the RBS's risk profile and to highlight trends, the BRC transitioned during the year to taking this report on a quarterly basis. A short form risk report was considered at all other meetings. • Received oral updates from the Chief Risk Officer and Chief Conduct and Regulatory Affairs Officer on the most current and material risks at each meeting. This enabled the BRC to discuss RBS's top risks and whether these were being managed effectively; whether RBS was operating within risk appetite; and whether business change was being managed effectively. • Held an in-depth session on risk reporting in October 2016 which led to additional recommendations for refinements to the form and content of reporting. Management will progress these improvements during 2017.
External developments	<ul style="list-style-type: none"> • Received reports from the Chief Risk Officer at each meeting highlighting external developments with the potential to affect RBS's ability to meet its strategic objectives or continue its operations. This included updates on the global economic environment, including developments in the US, Europe and China and associated impacts on financial markets; regulatory proposals for potential future capital requirements; and preparation for, and the impact of, the EU referendum result.
General Counsel's report	<ul style="list-style-type: none"> • The General Counsel reported to the BRC at each meeting on current and emerging key legal developments and risk and significant litigation risks affecting RBS.
US Risk Committee	<ul style="list-style-type: none"> • Received quarterly reports from the Chairman of the US Risk Committee on the key matters discussed at that forum. The US Risk Committee was established in May 2016 in response to US regulatory requirements and comprises Morten Friis as Chairman, the Chairman of the Board Risk Committee and the RBS Chief Financial Officer. It provides oversight of the risk management framework of RBS's combined US operations, including the review and approval of US risk management policies and material submissions to US regulators.
Strategic Risk	
Transformation	<ul style="list-style-type: none"> • Kept the execution risk of the RBS-wide transformation programme under review, receiving regular updates from the transformation team on progress, including independent opinions from Risk, C&RA and Internal Audit. • Considered progress against plan and reviewed interdependencies with other significant change programmes and key threats to delivery. In particular, the impact of the Williams & Glyn programme on transformation was monitored. Reviewed the impact of 2016 cost reductions and the 2017 budget restrictions on the programme. • Requested focus sessions on the controls transformation workstream, in particular the prioritisation and completion of the Risk and Control Assessments planned in 2016. A report was received from Internal Audit on the robustness of the assessments and the BRC will oversee management's plans to enhance processes and to remediate control weaknesses identified through completion of the exercise.
Williams & Glyn	<ul style="list-style-type: none"> • In Q1 2016, exercised oversight of the risks and challenges to the planned physical separation of assets in advance of the divestment of Williams & Glyn, confirming appropriate governance and assurance processes were in place for the programme. • Received independent reports on progress from Risk and Internal Audit, supplemented by independent third party assurance on progress. • Received updates on the wind-down of the separation programme after the decision of the Board not to proceed with this method of divestment and considered the impact of the decision upon people, costs, records management and security. Reviewed the impact of the change in strategic direction upon other key deliverables.
Ring-fencing Implementation plan	<ul style="list-style-type: none"> • Considered the key risks of the implementation of the ring-fencing programme as it moved from the design phase into execution in H2 2016, including reviewing the revised baseline plan and endorsing its submission to the PRA. • Oversaw the development of an integrated assurance programme involving Risk, Internal Audit and external third party assurance.

Report of the Board Risk Committee

Key area	Matters considered and action taken by the BRC
Strategic Risk	
Change Risk	<ul style="list-style-type: none"> Discussed the change risk profile of RBS and the prioritisation and impact of mandatory change programmes and considered the agreed risk appetite statement and measures used to assess change risk across RBS. Suggested refinements to the processes for assessing change risk and the acceptable volume of change.
Client Pricing for Assets and Liabilities	<ul style="list-style-type: none"> Reviewed the client pricing process against regulatory requirements to ensure that the pricing of liabilities and assets takes into account RBS's business model and risk strategy. The BRC noted that additional testing would be undertaken and enhancements made to the process. An annual review will be undertaken in future years.
Enterprise Wide Risk	
Risk appetite	<ul style="list-style-type: none"> Reviewed the risk appetite governance framework for 2016; provided feedback on the mechanism for managing and escalating breaches of risk appetite; and made suggestions in relation to simplification of the framework, before recommending this to the Board for approval. Reviewed risk appetite for strategic risks (earnings volatility, RBS-wide and functions, funding and equity investors) and subject to suggested refinements, recommended this to the Board for approval. Refreshed governance arrangements for material risks and put in place plans to transition to a Board approval framework for the most significant risks in 2017. This involved a number of in depth reviews of risk appetite throughout the year in relation to the following risk areas: tax, pensions, records management, payment processing, IT stability & resilience, people, reputational, traded market risk, non-traded market risk, business risk, financial reporting, legal entity risk, operational risk, information and cyber security, retail credit, mortgage risk, wholesale credit, commercial real estate, acquisition risk, settlement risk and conduct risk. Reviewed the cascade of RBS-wide risk appetite to franchises and functions and the alignment between strategic and material risk appetite statements. Considered the use of risk capacity (being the parameters within which risk appetite is set) and agreed risk capacity limits for strategic risks.
Stress testing	<ul style="list-style-type: none"> In Q1 2016, the BRC considered the results of the 2015 budget and forecast stress testing and reviewed Internal Audit's planned activity for assessing stress testing in 2016. During the year, the BRC considered the underlying assumptions and scenario selection for the external Bank of England stress test, including Internal Audit's opinion, making recommendations to the Board as appropriate. Provided challenge and scrutiny to the results of the three phases of the 2016 EBA stress test and the results of the 2016 Bank of England stress test. Reviewed the results of the reverse stress test and made recommendations to the Board in this regard. In H2 2016, the BRC considered the 2016 budget and forecast base and stress scenarios together with opinions from the three lines of defence and draft outputs and made recommendations to the Board in this regard. Oversaw enhancements to RBS's stress testing capability, in particular the remediation actions taken in response to the PRA review of stress testing capability.
Model risk framework	<ul style="list-style-type: none"> Oversaw the development of a new model risk framework designed to deliver improvements in the management of model risk. This included reviewing progress in remediating areas of identified weaknesses such as model validation and the restructure of model risk management team.
Integrated risk assessment process	<ul style="list-style-type: none"> Reviewed work undertaken by RBS to understand its risk culture and approaches to its assessment against a clearly articulated target culture. Considered the proposed Integrated Risk Assessment approach which was designed to provide a single approach to the assessment of risk mindsets and behaviours and risk capabilities leading to a more effective and simplified approach to the assessment of risk culture, the three lines of defence and performance assessments. The BRC reviewed the output of the pilot of the revised approach within certain functions and franchises and Risk.
RDAR	<ul style="list-style-type: none"> Monitored progress towards full compliance with the Basel Principles on Effective Risk Data Aggregation and Reporting (RDAR). Received a report from Internal Audit on material compliance with RDAR principles and oversaw communications with the PRA in this regard. The BRC will continue to ensure that areas requiring additional improvement are remediated in 2017 alongside plans to achieve full compliance.

Report of the Board Risk Committee

Key area	Matters considered and Action taken by the BRC
Enterprise Wide Risk	
Risk Assurance	<ul style="list-style-type: none"> Received quarterly reports on issues highlighted by reviews conducted in each of the three franchises by Credit Quality Assurance, Market Quality Assurance, Control Assurance and a newly created Stress Testing Assurance team.
Market, Credit and Operational Risk	
Credit, Market and Operational risk MI	<ul style="list-style-type: none"> Reviewed RBS's risk profile relative to credit, market and operational risk, and examined detailed management information (MI) within the Risk Management report in this regard.
Control Environment Certification	<ul style="list-style-type: none"> Received bi-annual reports on the Control Environment of the franchises and functions and sought management's assurance that appropriate measures were in place to ensure that the businesses could continue to operate safely, where control weaknesses had been identified.
NatWest Markets (formerly CIB) Control Environment Remediation	<ul style="list-style-type: none"> Reviewed and challenged management plans to remediate and strengthen the conduct and control environment across the NatWest Markets franchise. Received reports on specific remediation issues and control issues including, Trade and Transaction Reporting; Collateral Management Algorithmic Trading and Intra-Day Risk; IMA waiver and capital implications; and surveillance measures and potential enhancements. Reviewed management's transformation plans for the business, including how these would impact remediation, mandatory change and the control environment. Received reports following challenge by the second line of defence and the Technical Executive Risk Forum of management's views of progress against expected outcomes.
Payments	<ul style="list-style-type: none"> Received progress reports in relation to the payments transformation programme, designed to remediate weaknesses in the payments infrastructure and provide a platform to support mandatory change. Requested updates on compliance with the Payment Card Industry Data Security Standards and Wire Transfer Regulations (WTR) and considered an Internal Audit report on WTR compliance.
Resilience, security and cyber risk	<ul style="list-style-type: none"> The BRC received bi-annual reports on security and resilience and requested a separate update on cyber security. This included a report on the controls and defences in place, an update on improvements identified via RBS's participation in CBEST (a cyber testing initiative led by the Bank of England), and a summary of the alignment of the RBS's security policy with the ISO standards.
Material credit exposures	<ul style="list-style-type: none"> Oversaw the Executive Credit Group (ECG) receiving a summary of the decisions made by the ECG in the period. Reviewed the most material credit decisions made in 2015 and examined trends in the market. Approved a revised governance for large credit exposure decisions, designed to enhance the level of BRC and Board oversight.
Other operational risks	<p>The BRC also reviewed reports in relation to:</p> <ul style="list-style-type: none"> the potential risks posed by end of life software; simplification of the RBS Policy Framework. The BRC requested that greater analysis of the volume of exceptions to policy be undertaken; and data quality. Following review of progress against a detailed plan, the BRC was pleased to note significant progress in this area.
Capital and Liquidity Risk	
ICAAP and ILAAP	<ul style="list-style-type: none"> In Q2 2016 the BRC reviewed the draft Internal Capital Adequacy Assessment process (ICAAP) along with an Internal Audit review and recommended the document to the Board for approval subject to certain enhancements. In Q3 2016 the BRC reviewed both the scenarios assumptions for the 2016 Internal Liquidity Adequacy Assessment Process (ILAAP) and the final ILAAP submission and, after due consideration, recommended them to the Board.
Recovery and Resolution planning	<ul style="list-style-type: none"> Oversaw the first part of a two year remediation process in designed to deliver a recovery plan in line with industry best practice. Examined and commented upon the draft 2016 recovery plan and resolution pack and recommended them to the Board for approval. Approved the final version of the recovery plan under delegated authority from the Board.
Capital Management	<ul style="list-style-type: none"> Reviewed the progress of the capital management capability enhancement programme. Received an update on proposed regulatory changes to capital requirements and noted the areas most likely to be impacted and the likely implementation timescales.

Report of the Board Risk Committee

Key area	Matters considered and Action taken by the BRC
Capital and Liquidity Risk	
Legal entity control & risk framework	<ul style="list-style-type: none"> Held a detailed session on the internal finance and risk processes relating to subsidiary legal entities in June 2016 and considered an update on the legal entity operating model later in the year, with a particular focus on specific enhancements being developed to improve the robustness of the legal entity control and risk framework. Supported management's plans to create an RBS-wide programme to build legal entity capability and deliver a coordinated framework focusing on specific legal entity control and assurance requirements.
Conduct, Regulatory and Remediation	
Representations to Regulators	<ul style="list-style-type: none"> Reviewed the assurance and governance in place to support representations to regulators. Reviewed attestations requiring Board level approval, including a US Volcker Rule attestation and representations relating to controls in place within the FX business.
Financial Crime	<ul style="list-style-type: none"> Discussed the Group Money Laundering Reporting Officer's (MLRO) Annual Report 2015 and recommended it to the Board.
Other conduct risks	<p>The BRC also reviewed reports in relation to:</p> <ul style="list-style-type: none"> the European Markets Infrastructure and Markets in Financial Instruments regulations; progress to meet the requirements of the European Deposit Guarantee Scheme; RBS's and NatWest's compliance with the FCA client assets rules (CASS) and recommended the reports to the Board for approval; the New Product Risk Assessment (NPRA) process; complaints performance improvement; and individual regulatory investigations and remediation.
Risk and Conduct & Regulatory Affairs	
	<ul style="list-style-type: none"> Oversaw the performance and the independence of the Risk and Compliance functions, through undertaking bi-annual visits to Risk and Conduct & Regulatory Affairs during which the BRC considered people and succession planning, budget and the resource capability of both functions. Received quarterly dashboards of key management information covering headcount, comparisons to budget, high performing staff turnover and outputs of staff surveys. Assessed the performance of the Chief Risk Officer and Chief Conduct & Regulatory Affairs Officer.
Accountability and Remuneration	
	<p>Continued to provide oversight over the risk dimension of performance and remuneration arrangements, working closely with the Group Performance and Remuneration Committee. The Report of the Group Performance and Remuneration Committee on pages 87 to 111 includes further detail on how risk is taken into account in remuneration decisions. Key matters considered by the BRC included:</p> <ul style="list-style-type: none"> accountability recommendations in respect of significant material events; the risk and control objectives of members and attendees of the RBS's Executive Committee, with additional focus on underlying objectives for the Chief Risk Officer and the Chief Conduct & Regulatory Affairs Officer; an assessment of the risk/conduct performance of members and attendees of RBS's Executive Committee, with recommendations made to the Group Performance and Remuneration Committee as appropriate to inform its decision on pay and awards; an assessment of the risk/conduct performance of the RBS and its businesses, with recommendations made to the Group Performance and Remuneration Committee to inform its decision on adjustments to the annual bonus pools; performance conditions for the RBS's Long Term Incentive Plans and assessment of proposed vesting levels to ensure risk management/conduct performance is fairly reflected in vesting outcomes; and the proposed Executive Director Future Remuneration Policy as detailed on pages 94 to 99 from a risk and control perspective.

Baroness Noakes
Chairman of the Board Risk Committee

Report of the Sustainable Banking Committee

Letter from Penny Hughes Chairman of the Sustainable Banking Committee



“Our brand strategy reflects our drive to build a customer focused bank which our people can be proud of and our customers trust”

Dear Shareholder,

The Sustainable Banking Committee (SBC) is primarily concerned with overseeing, supporting and challenging actions taken by management to promote RBS as a sustainable business, capable of generating long term value for its stakeholders.

Despite a challenging year for the Bank in general, we have made progress on our agenda to build a more sustainable bank. The SBC continues to focus on culture, customers, people, brand & communications and environmental, social and ethical (ESE) issues. Engagement with management continues to be good and we have listened, learnt and acted on challenges and ideas from stakeholders we have spoken to throughout the year.

Our ambition to be number one for customer service, trust and advocacy in each of our chosen business areas remains unchanged. Delivering this ambition depends on our ability to demonstrate beyond question that we are a responsible company, that has learnt from the past, doing business in a sustainable way.

We will earn trust by putting customers first, making RBS a great place to work, supporting our communities, and being mindful of environmental impacts.

Progress made in 2016 includes:

- furthering the integration of sustainable banking into our core businesses and increasing transparency of this with the integration of our previously separate Sustainability Report into the main Annual Report;
- encouraging the development of the sustainable banking strategy, meeting the needs of all our stakeholders whilst aligning with RBS's overall strategy;
- overseeing how management is embedding culture and Determined to lead standards within our employee value proposition;
- overseeing the brand strategy to reposition Royal Bank of Scotland, NatWest and Ulster Bank for customers;
- posing and addressing key challenges with management such as the provision of free banking, supporting enterprise and supporting companies or individuals to seek alternative finance when RBS is unable to help;

- challenging management's efforts on meeting the needs of particular customer groups such as high net worth individuals and small and medium sized enterprises;
- ongoing commitment to both internal and external stakeholder engagement through face to face sessions and visits to customer facing businesses;
- reviewing our progress on environmental targets; and
- reviewing complaint handling and the strategy to identify root cause and resolution.

The efforts to build a responsible and sustainable business are being recognised through independent and external measures. We retained our place in the Dow Jones World Sustainability Index with our highest score to date (84) and achieved a leadership category listing in the Carbon Disclosure Project Index (A-).

We are also increasingly being recognised as an attractive employer. RBS was shortlisted at the 2016 National Diversity Awards as well as being shortlisted for Outstanding Employee Network Group of the Year in the European Diversity Awards. We recently came 13th in Stonewall's top 100 employers, up from 32nd last year.

The SBC has also seen tangible evidence of good customer outcomes. RBS is the largest lender to small and medium sized business in the UK and gross lending to our Personal and Business Banking customers is up 29% year on year. Building financial capability remains a focus for RBS with financial health checks available to Personal and Business Banking customers. MoneySense, our flagship financial education programme for 5 – 18 year-olds, also continues to grow. Raising awareness of the importance of financial education was supported by a NatWest national advertising campaign last year, along with a new commitment to reach another one million young people with MoneySense by the end of 2018.

The repositioning of our primary customer brands was a significant moment for RBS. The SBC played a role in overseeing and challenging the brand strategy which plays an important role in building a customer focused bank which our people can be proud of and our customers trust.

Over a number of years RBS has experienced a shift by setting out a clear and simple purpose and defining our Values. We have restructured our business, made progress on our service proposition but acknowledge there is more to do, introduced the YES Check and made changes to the way we do some of the fundamentals of banking. The SBC will continue to operate at a strategic level to support management on its journey to reaching our ambition to becoming a more sustainable and truly customer focused bank.

My thanks go to the SBC members and attendees for their contribution and support through another challenging year.

Penny Hughes
Chairman of the Sustainable Banking Committee
23 February 2017

Report of the Sustainable Banking Committee

Report of the Sustainable Banking Committee

Meetings

The Sustainable Banking Committee held six scheduled Committee meetings in 2016 which were attended by the Chief Executive, Chairman, senior representatives from the customer-facing franchises as well as Human Resources, Sustainability, Risk, Conduct & Regulatory Affairs, Communications & Marketing, and Strategy.

Stakeholder engagement sessions

In addition to ongoing engagement which takes place across our business each day, the Committee has run a proactive engagement programme since 2011 to which we invite external stakeholders to meet with, and challenge, the most senior decision makers in RBS.

We have met with over 50 different groups of NGOs, civil society groups, government bodies, consumer groups and investors in this way and the purpose is to listen and understand where RBS could do more. These discussions help shape future policies, influence strategic priorities and inform decision making across RBS on our journey to becoming a customer focused bank.

In 2016 we held four such stakeholder engagement sessions covering the following topics:

- how to serve and support scale-up, high growth customers beyond start up stage;
- defining the vision of sustainable banking for RBS and taking a bolder, more integrated approach to delivering it;
- financial capability and the key concerns and challenges faced by Irish consumers in relation to their personal finances; and
- what does sustainable banking mean for our culture, our behaviour, our people and our customers?

Following the sessions we identify opportunities for follow up and further engagement. In December, we welcomed back a number of our past guests to share the progress made and invited further challenge and alternative perspectives.

As part of its programme of stakeholder engagement, members of the SBC undertook a visit to Personal and Business Banking which provided valuable insight to the SBC. There are plans for more frontline customer engagement in 2017.

Membership

The Sustainable Banking Committee comprises four independent non-executive directors. The Chairman and members of the SBC, together with their attendance at meetings, are shown below.

	Attended/ scheduled
Penny Hughes (Chairman)	6/6
Alison Davis	6/6
Robert Gillespie	6/6
Mike Rogers (1)	5/5

Note:

(1) Appointed to the committee on 25 April 2016

Performance evaluation

The annual review of the effectiveness of the Board and its senior Committees, including the Sustainable Banking Committee, was conducted internally in 2016. The Committee has considered and discussed the outcomes of this evaluation and accepts the findings. Overall the review concluded that the Sustainable Banking Committee continued to operate effectively.

In particular, during 2016 the Committee focused on being more forward looking and strategic with its time, focusing on priorities of culture, people, customer, brand & communications and ESE issues. The stakeholder engagement sessions are regarded as a valuable opportunity to learn how well RBS is aligned to external sustainability priorities. During 2017, the Committee will continue to focus on these priorities, and ensure it undertakes a proactive programme of stakeholder engagement.

The outcomes of the evaluation have been reported to the Board and the Committee will track progress during the year.

Role and responsibilities of the Sustainable Banking Committee

Authority is delegated to the Sustainable Banking Committee by the Board and the SBC reports and makes recommendations to the Board as required. The terms of reference of the SBC are available on rbs.com and these are reviewed annually and approved by the Board. A report on the activities of the SBC in fulfilling its responsibilities is provided to the Board following each meeting. The principal responsibilities of the SBC are shown below:

Culture

- receive updates on actions to drive the Board approved culture;
- oversee progress on standards, competence and capability

People

- oversee the Employee Value Proposition and initiatives to ensure a diverse workforce which feels clear, capable and motivated;

Customer

- oversee customer centricity priorities and how RBS is supporting and engaging with key customer segments;
- oversee progress being made to achieve the long term target of being number one for customer service, trust and advocacy in each of our chosen businesses;

Brand & Communications

- oversee the brand strategy in moving to a bank of brands approach focusing on building equity in our customer brands;
- oversee actions being taken by management to manage RBS's reputation;

ESE Issues

- receive reports on managing ESE risk;
- consider RBS's environmental footprint and how RBS is operating in its communities; and
- consider activities being undertaken to support the "green" economy.

Directors' Remuneration

	Page
Annual statement from the Chairman of the Group Performance and Remuneration Committee	88
Key features of the new remuneration policy for executive directors	89
Comparison of the current and new remuneration policy for executive directors	90
Questions and answers on the new remuneration policy	92
Wider employee considerations	93
Directors' Remuneration Policy	
Policy table for current executive directors	94
Remuneration scenarios for current executive directors	96
Policy table for the Chairman and non-executive directors	97
Discretion	97
Recruitment remuneration policy	98
Consideration of employment conditions elsewhere in the company	98
Consideration of shareholders' views	98
Service contracts and policy on payments for loss of office	99
Annual report on remuneration	
Implementation of policy in 2017	100
Total remuneration paid to executive directors for 2016	101
Assessment of long-term incentive (LTI) awards	101
LTI awards granted during 2016	102
Performance conditions for 2017 LTI awards	103
Payments to past directors	104
Total remuneration paid to the Chairman and non-executive directors for 2016	104
Directors' interests in shares and shareholding requirements	105
Total Shareholder Return (TSR) performance	106
Pay comparisons	106
The Committee and its activities during 2016	107
Shareholder voting on the remuneration policy	108
Other Remuneration Disclosures	
Eight highest paid senior executives below Board	109
Remuneration process and adjustments for risk, malus and clawback	109
Remuneration policy for all employees	110
Remuneration of Material Risk Takers	111

Directors' Remuneration Report

Annual statement from Sandy Crombie
Chairman of the Group Performance and Remuneration Committee



“the focus is on meaningful, long-term shareholding as the mechanism for achieving alignment with shareholders”

Dear Shareholder,

I am pleased to set out the Directors' Remuneration Report for 2016. This report describes the pay decisions that we took for the last financial year and the new remuneration policy that is being proposed to shareholders for approval at the forthcoming AGM.

Policy developments in 2016

I know that views on executive pay are continuing to evolve. The government is consulting on areas of reform aimed at strengthening the UK's corporate governance arrangements. A separate industry-led Executive Remuneration Working Group has also set out areas where it is believed that improvement is needed to restore trust in current remuneration practices. RBS continues to contribute to consultations aimed at strengthening governance and pay arrangements.

It is clear many shareholders value simple remuneration structures. The Committee spent a great deal of time considering alternative constructs and how these would align to RBS's cultural aims on pay. The proposed new policy represents a significant change and has two principal aims: to produce greater alignment with shareholders and to discourage the potential for excessive risk taking.

The design focuses on creating alignment by ensuring executives build up larger shareholdings and retain them for longer. This intent is being reinforced by a significant increase in shareholding requirements from 250% to 400% of salary for the Chief Executive and from 125% to 250% for the Chief Financial Officer. The new policy also encourages sustainable long-term performance by having a lower maximum long-term incentive award level, but with performance assessed on factors that the executive would reasonably be expected to achieve, creating a less leveraged construct and encouraging safe and secure growth. The maximum potential long-term incentive award is being reduced by around 40% for the Chief Executive and by around 30% for the Chief Financial Officer.

It is also proposed that pro rating of long-term incentive awards will not apply for good leavers under the new policy. The Committee recognises that time pro rating is a common preference for some investors and its removal has only been included after considerable thought, and after consulting with a number of shareholders. The intention is to create high levels of shareholding that persist for a period after leaving and pro rating of awards reduces this alignment. RBS is unusual in having no annual bonus element of pay for executive directors and bonus awards would typically not be subject to pro rating. Furthermore, the policy aims broadly to maintain the expected value of pay to executive directors over their typical tenure in role.

This aim is achieved through a combination of reduced award levels, performance factors that are designed to be more within the control of management and the removal of pro rating for good leavers. The circumstances that would be considered for good leaver treatment are set out in more detail in this report.

No change is proposed to the quantum of fixed pay, although fixed share allowances will be released over three, rather than five years to create a more even release of value across fixed and variable pay. A further development is that the pension allowance under the recruitment policy for new executive directors will be reduced from 35% to 25%, bringing the rate closer to that of the wider employee population.

In summary, the focus is on meaningful long-term shareholding as the mechanism for achieving alignment with shareholders. To date, the proposed remuneration policy has been well received in discussions with our largest shareholders.

Considerations for other employees

The Committee recognises that RBS will only achieve its ambitions if all employees are engaged, motivated and supported by appropriate remuneration structures. Average salaries for our UK employees have increased by 7.5% over the last three years while executive directors' salaries have been static. Our rates of pay continue to exceed the living wage and we have removed sales incentives for front line retail staff and increased fixed pay so that they can concentrate on providing great customer service.

Financial performance in 2016

Some important milestones were met in 2016. RBS was able to retire the Dividend Access Share in March and this was a key part in normalising RBS's capital structure. Good progress has also been made in resolving a number of major legacy and conduct issues although these continue to affect financial results. Variable pay across RBS is subject to a robust performance assessment process which allows outcomes to be adjusted if risk management or conduct has fallen short of the required standard.

The restructuring of the business has continued during 2016 but there is a strong business at the heart of RBS, capable of delivering sustainable returns for shareholders. The franchises have performed well with adjusted operating profits of £4,249 million for 2016. The Committee's decisions aim to strike a balance in rewarding employees for good performance but recognising RBS is not yet in the position that it needs to be.

Pay decisions for 2016

The Group bonus pool has fallen from £373 million in 2015 to £343 million in 2016, a reduction of 8%. Over 93% of this pool will be paid to those below the executive level. Where employees do receive a bonus, the average amounts remain relatively modest with 50% of employees receiving £2,000 or less and a further 23% receiving less than £5,000. The amount of any immediate cash bonuses continues to be limited to £2,000.

The report sets out further information and I hope shareholders will support the resolutions on remuneration arrangements at the forthcoming AGM. I am very grateful for the guidance and support provided by my fellow Committee members as well as those who assist the Committee over the year. I would also like to thank shareholders for their constructive input as we discussed how best to shape the remuneration policy for the years ahead.

Sandy Crombie
Chairman of the Group Performance and Remuneration Committee
23 February 2017

Directors' Remuneration Report

Key features of the new remuneration policy for executive directors

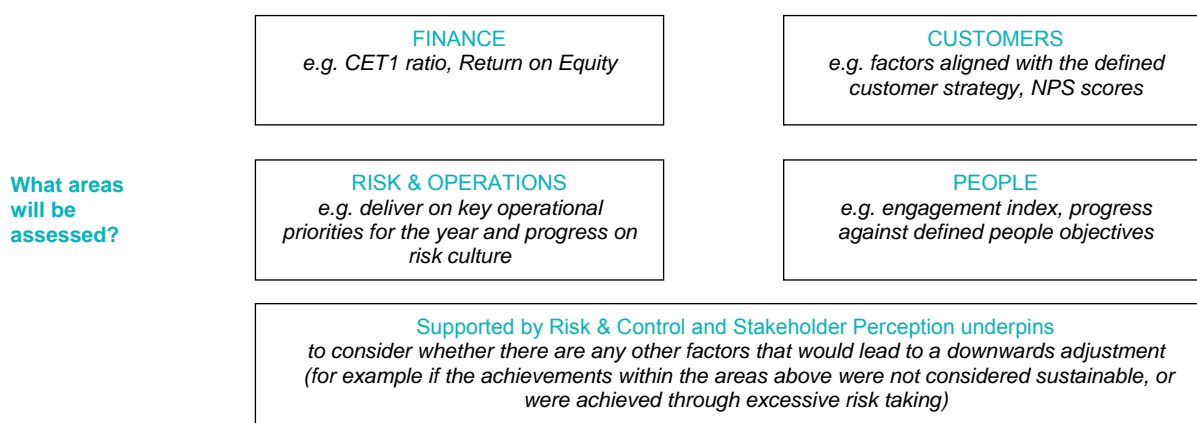
Key features	<p>The new policy is focused on the long term, aimed at attracting and keeping the right people for RBS.</p> <p>The intent is a policy that aligns executives with shareholders predominantly through holding shares rather than formulaic and unpredictable performance conditions.</p> <p>As a result, shareholding requirements will be significantly increased under the new policy and performance testing of LTI awards will be based on factors that executive directors would reasonably be expected to achieve, encouraging executives to operate within risk appetite.</p> <p>The maximum quantum will be reduced in line with a growing consensus on the need to restrain executive pay.</p> <p>The intention is to create a construct that is more highly valued by executives, by assessing performance on factors considered to be more within the control of management and therefore providing greater certainty of outcomes.</p> <p>Combined with the removal of pro rating for good leavers, the expected value of remuneration delivered to executive directors over time is broadly maintained.</p> <p>Longer vesting and retention periods will apply to LTI awards, with the release of shares over an eight year period, helping to ensure decisions and outcomes reflect a truly long-term timeframe and are even further aligned with the experience of shareholders.</p>
---------------------	--

How will performance assessment work under the proposed LTI construct?

For each of the core performance areas of Finance, Risk & Operations, Customers and our People, the Committee will consider whether the executive director has over the relevant period achieved what would reasonably have been expected in the circumstances. The Committee will review performance against factors (examples are set out below) relevant to RBS's strategic objectives in each area, but will apply its judgement without reference to formulaic targets. Performance will be assessed taking into account circumstances applying over the period of assessment which may have affected the achievability of performance objectives. The majority of the performance variation will take place under a pre-grant test, with a pre-vest assessment representing a final check that, taking all circumstances into account, overall performance has been satisfactory. The achievement of reasonable or 'target' performance expectations will deliver full, or nearly full, payout of the LTI awards, reflecting the significantly reduced level of awards.

Each year, the performance factors will be determined in light of RBS's priorities for that year. The first awards will not be made under the proposed LTI construct until early 2018 and further details will be disclosed in the 2017 annual remuneration report.

Performance management framework



The pre-grant test will constitute a collective and individual view of performance over the prior year. No deduction will be made for target performance. Prior to vesting, a pre-vest test will be based on an assessment of collective performance for the year for which the award was made, knowing 'what we know now', and taking into account all circumstances. This is intended to carry a high degree of certainty, and to vest as long as a threshold level of sustainable performance has been delivered.

The aim is to reward sustained performance and, following the application of both the pre-grant and pre-vest assessment, executive directors should expect to receive 80% of the award on average over time provided that they deliver on the performance factors as determined by the Committee. Awards may be reduced, potentially down to zero, further to the application of either the pre-grant or pre-vest tests where there has been significant underperformance or risk management failings.

Directors' Remuneration Report

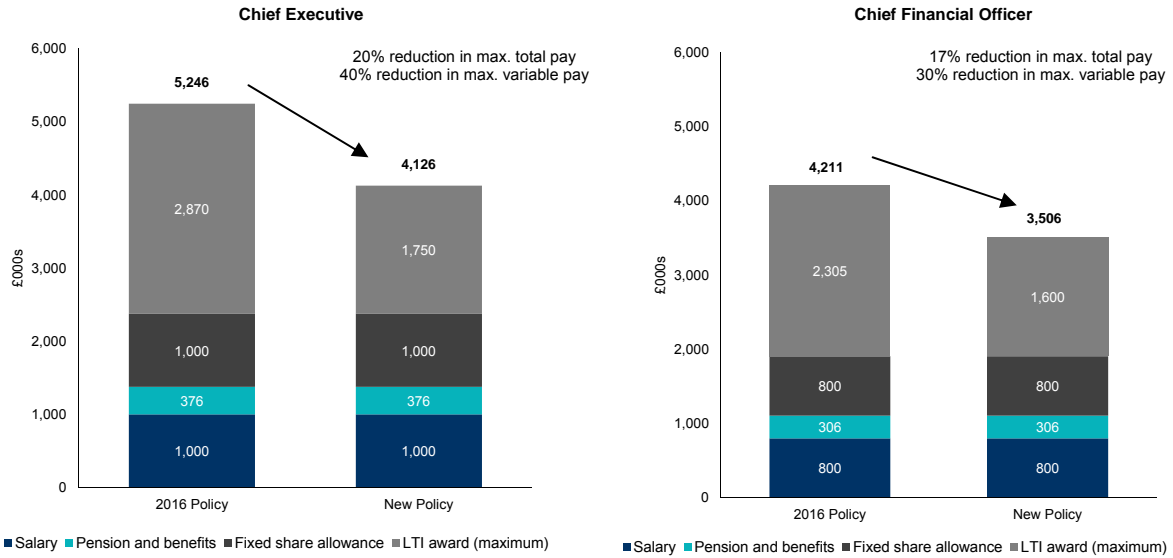
Comparison of the current and new remuneration policy for executive directors

	Current policy	New policy
<p>Fixed remuneration</p> <p><i>overall, no change in quantum at this time</i></p>	<p>Salary £1,000,000 for the Chief Executive £800,000 for the Chief Financial Officer</p> <p>Fixed share allowance 100% of salary, delivered in shares released over a five year retention period.</p> <p>Pension allowance 35% of salary, delivered in cash.</p> <p>Standard benefit funding £26,250</p>	<p>No changes to salary levels are proposed at this time.</p> <p>No change to the fixed share allowance amount but shares will be released over a three year retention period, to create a more even release structure between fixed and variable pay.</p> <p>No change to pension allowance for current executive directors. Policy for new executive directors to be reduced to 25% of salary.</p> <p>No changes to standard benefit funding level.</p>
<p>Variable remuneration</p> <p><i>significant reduction in maximum potential</i></p>	<p>Long-term incentive award Underlying award of 400% of salary but with pay-out capped by regulatory maximum which for performance year 2016 equates to 287% of salary.</p> <p>Pre-vest performance measures based on four categories: Economic Profit, Relative TSR, Safe & Secure Bank and Customers & People together with a risk and conduct underpin.</p> <p>A three year performance period and the award vests in equal amounts in years four and five.</p> <p>A six month retention period applies after vesting and the clawback period is seven years from the date of grant.</p>	<p>175% of salary for the current Chief Executive (currently £1.75 million) and 200% of salary for the current Chief Financial Officer (currently £1.6 million).</p> <p>Pre-grant and pre-vest tests, to consider performance in the round, against what would reasonably have been expected in the areas of Finance, Risk & Operations, Customers and our People. Risk & Control and Stakeholder Perception underpins will apply.</p> <p>Extension of the deferral period with vesting taking place in equal amounts over years three to seven.</p> <p>A 12 month retention period applies after vesting. The clawback period is extended to ten years from grant if events are under investigation at the end of the seven year period.</p>
<p>Other elements</p> <p><i>better alignment with shareholders</i></p>	<p>Shareholding requirement 250% of salary for the Chief Executive 125% of salary for the Chief Financial Officer</p> <p>A period of five years is allowed in which to build up shareholdings to the required level. Any unvested share awards are excluded from the calculation.</p> <p>Leaver treatment LTI awards held by good leavers are normally pro rated based on time served during the performance period.</p>	<p>400% of salary for the Chief Executive 250% of salary for the Chief Financial Officer.</p> <p>Unvested LTI awards will count towards the requirement once any pre-vest performance has been assessed, three years after grant. The number of unvested shares that count will be reduced to reflect the estimated tax liability arising on vesting. Once shares are free from their respective retention periods, executive directors will be permitted to sell a maximum of 25% of such shares until the requirement is met. It is estimated that it would take a new Chief Executive five years to meet the 400% shareholding requirement.</p> <p>Executive directors will continue to hold significant shareholdings after leaving and a post-employment shareholding requirement is therefore not considered necessary. Depending on leaver circumstances, it would take between three and eight years for an executive director to fully dispose of RBS shares due to the long vesting and retention periods.</p> <p>Future LTI awards held by good leavers will not be subject to pro rating for time. Removal of pro rating is a key part of the construct in order to achieve the reduction in maximum opportunity while broadly maintaining expected value to executive directors over their typical tenure in role. It also helps to ensure that individuals retain an appropriate long-term focus right up to the point of departure, as well as providing greater shareholder alignment post employment.</p>

Further details on the new remuneration policy and arrangements for the year ahead can be found in the relevant sections of this report.

Directors' Remuneration Report

Change in maximum remuneration opportunity

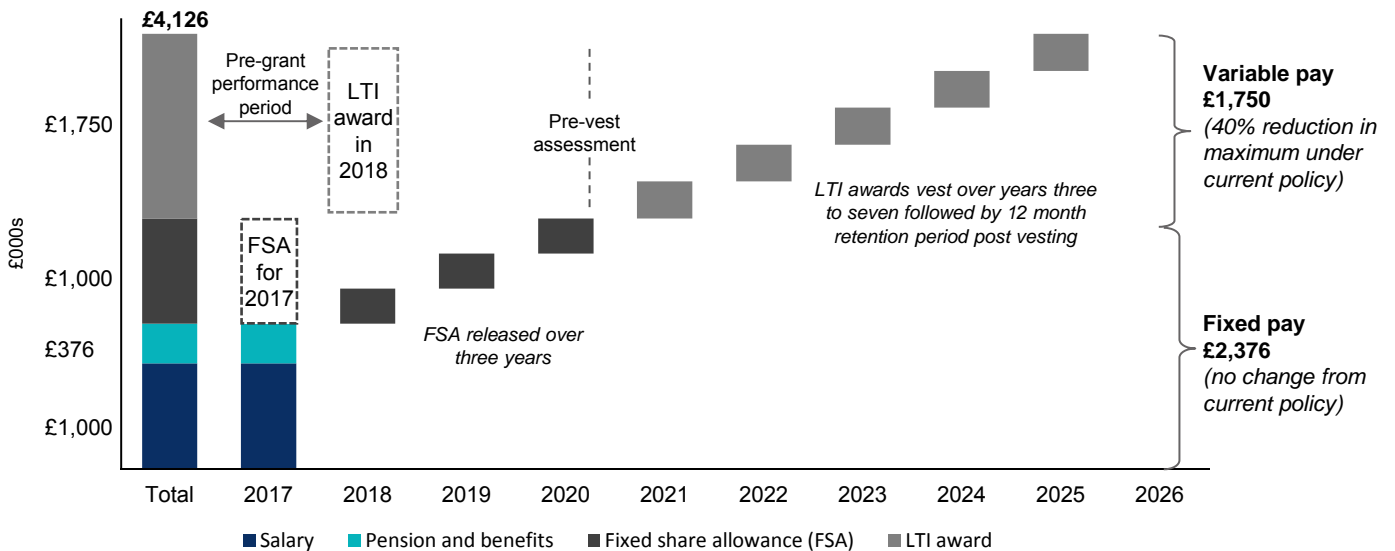


Expected target value of remuneration

The new remuneration policy promotes sustainable long-term performance by having a lower maximum LTI award level and performance tests that encourage individuals to operate within risk appetite. The release of shares will extend over an eight year period (vesting over seven years and one year post-vesting retention period), following a year of pre-grant assessment to determine the size of the award.

While the maximum and expected value of pay from a single year's remuneration is being reduced, the policy aims broadly to maintain the expected value of pay to executive directors over their typical tenure in role. The combination of reduced LTI award levels, offset by performance based on factors that the executive would reasonably be expected to achieve and the removal of pro rating for good leavers ensures this aim is achieved.

Timing of remuneration payments – based on the Chief Executive for the 2017 performance year



Directors' Remuneration Report

Questions and answers on the new remuneration policy

Why are changes being made to the policy at this time?

The current remuneration policy was approved by shareholders at the 2014 AGM for a period of three years and is therefore due for renewal at the 2017 AGM. During 2016, the Committee took the opportunity to assess how the remuneration policy could best fit with RBS's culture and pay philosophy for employees.

What options did the Committee consider?

During 2016, the Committee reviewed the current policy against a range of factors including the latest guidance from shareholders, regulatory requirements, the external environment and wider social considerations in determining executive pay.

Two main options were identified following the review:

- Adopting an alternative LTI construct to replace the current structure, based on reduced maximum quantum but with performance assessed on factors that the executive would reasonably be expected to achieve; or
- Keeping the current construct with changes limited to those required to comply with regulatory requirements.

After consultation with major shareholders, the Committee believes that the alternative LTI construct provides the best fit with RBS's ambitions as well as being strongly aligned to the creation of long-term shareholder value.

What material factors are taken into account when setting remuneration policy?

The intention is to create a remuneration policy that is specific to RBS and its particular circumstances rather than looking to follow standard market practice. The policy aims to reinforce our values and support the delivery of RBS's strategy. The views of shareholders are key in shaping the remuneration policy along with the need to comply with evolving regulatory requirements. The Committee also looks to ensure consistency, where possible, between the executive director policy and pay proposals for the broader employee population. This includes less reliance on variable pay and the use of deferral in shares, malus and clawback to ensure that any variable pay that is awarded is aligned with long-term performance.

What are the key features of the new policy?

RBS-driven features:

- Maximum potential LTI awards will be reduced;
- Performance assessment is based on factors considered to be more within the control of management;
- The policy encourages executive directors to operate within risk appetite and deliver safe and secure growth;
- Shareholding requirements will be increased;
- Fixed share allowances will be released over a three year rather than a five year retention period, in recognition of the impact of the extended deferral period for LTI awards;
- LTI awards held by executive directors who leave in 'good leaver' circumstances will not be subject to time pro rating, helping to maintain expected value and increasing post employment shareholder alignment; and
- The pension allowance under the recruitment policy for new executive directors will be reduced from 35% to 25% of salary, with a corresponding increase to other elements of fixed pay.

Regulatory-driven features:

- Pre-grant performance tests will be introduced;
- The pre-grant performance test has the effect of preventing the grant of an LTI award in the year of joining;
- The deferral period will be extended with awards vesting between years three to seven from the date of grant;
- The retention period that applies after the vesting date will be increased from six months to twelve months; and
- The clawback period is extended to ten years from grant if events are still under investigation after seven years.

Why will future LTI awards not be subject to pro rating?

The new policy takes into account the significant reduction in maximum opportunity and the regulatory restriction which has the effect of preventing the granting of LTI awards in the first year of employment. The Committee believes that removal of time pro rating for good leavers is fair in order to broadly maintain the expected value of pay over time and is appropriate in RBS's particular circumstances.

RBS is unusual in having no annual bonus element of pay and bonus awards would typically not be subject to pro rating. Under an LTI only construct, removal of pro rating helps to ensure that executive directors are motivated and retain an appropriate long-term focus right up to the point of departure, and also provides greater shareholder alignment and continued accountability for decisions post employment. The departing good leaver retains exposure to RBS shares for up to eight years post leaving due to the long vesting and retention periods that continue to apply.

The removal of pro rating places additional focus on good leaver definitions and further details on the circumstances that will qualify for good leaver treatment are set out on page 99.

When will the new policy be implemented?

Subject to approval from shareholders, the new policy will be effective from the date of the AGM. The changes will be implemented in a transitional period from 2017 to 2018. The fixed share allowance for 2017 will be awarded after the AGM, to be released over a three year retention period, and the first LTI awards under the new policy will be made in early 2018.

How will LTI awards be made in 2017?

The LTI award to be made in March 2017, for the 2016 performance year, will be the last award made under the existing remuneration policy. This award will include a longer deferral period, with 50% of the award vesting after four years and the remaining 50% vesting in years five to seven, along with an extended clawback period in line with regulatory requirements. Further details for 2017 can be found on page 100 and a summary of the transitional arrangements is set out below.

Awarded in 2017	Awarded in 2018
2017 salary	2018 salary
2017 pension	2018 pension
2017 fixed share allowance (released over 2018-2020)	2018 fixed share allowance (released over 2019-2021)
Current policy LTI for 2016 performance year (vests 50% in 2021, 50% split over 2022-2024)	New policy LTI for 2017 performance year (vests pro-rata over 2021-2025)

Directors' Remuneration Report

Wider employee considerations

To provide the best possible customer service, RBS is building a strong, simple and fair bank. Performance and pay management is part of that process.

RBS needs to build an engaged and inclusive workforce, capable of providing excellent customer service.

- Senior leaders are subject to individual and collective performance assessment based on factors which include financial strength and customer service.
- RBS has set a target for each Executive Committee member to have at least 30% women in senior roles (the top three leadership layers) by 2020.
- Gender targets are one of three People measures, together with engagement and leadership, which are considered when assessing performance for some of our senior leaders.
- Employees are motivated by good leadership and almost 16,000 employees undertook our 'Determined to Lead' leadership programme in 2016.
- We have now trained over 60% of employees at all levels of RBS to tackle unconscious bias, helping to remove bias in our recruitment processes, build more inclusive teams, make well informed decisions and better understand and serve our customers.
- In October 2016 we launched Service Excellence, our new customer service programme with over 34,000 employees receiving training so far.
- Professional Standards Frameworks set out the relevant knowledge, skills, and behaviours expected of RBS employees to embed good conduct.
- While employee engagement has been impacted during 2016 by the ongoing restructuring of the business, it remains higher than when we set out our strategic plan in 2014.

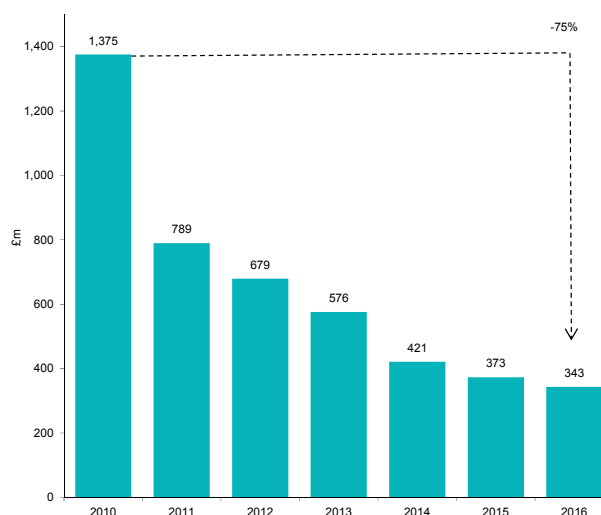
RBS is simplifying how employees get paid.

- In Personal & Business Banking, pay for frontline roles is linked to supporting customers, rather than short-term incentive schemes, and this was extended to employees in Ulster Bank with effect from 1 January 2017.
- Our clerical population in the UK and Republic of Ireland now receives only fixed pay, making pay arrangements easier to understand.
- Salary ranges have been updated to reflect the external market and to ensure that people doing the same or similar roles are paid more consistently.

The Committee must ensure that good behaviours are encouraged and that conduct issues are accounted for.

- The policy aims to pay people appropriately for their work and commitment to serve customers well.
- RBS continues to operate as a fully accredited living wage employer.
- If conduct falls short of the standard expected, the Committee can adjust variable pay awards through malus (reduction or cancellation of awards prior to payment) or clawback (recovering awards that have already been paid).
- Further information on the accountability review process under which malus and clawback can be applied is set out later in this report.
- The Committee aims to strike a fair balance between adjustments to variable pay as a targeted measure to change behaviour whilst not disproportionately penalising employees who are not directly responsible for events.
- As set out below, bonuses have continued to shrink at RBS, aligned with the restructuring that has taken place and the actions taken by the Committee.
- Pay levels reflect the progress made in 2016 and the bank that RBS is becoming, while ensuring our people are fairly and appropriately rewarded for the work they do.

Bonus pool reduced steadily from 2010 to 2016



Directors' Remuneration Policy

Directors' Remuneration Policy

A new Directors' Remuneration Policy is being proposed to shareholders at the forthcoming Annual General Meeting (AGM). Subject to approval being received, the policy will be effective from the date of the 2017 AGM. The policy will apply for three years, until the AGM in 2020, unless changes are required in which case a revised policy will be submitted to shareholders for approval. The objective of the policy is to support the business strategy and promote the long-term success of RBS.

Fixed pay elements for current executive directors

Fixed pay elements are intended to provide a level of competitive remuneration for performing the role. The intention is to have less reliance on variable pay and thus discourage excessive risk-taking.

Element of pay	Purpose and link to strategy	Operation	Maximum potential value
Salary	<p>To aid recruitment and retention of high performing individuals whilst paying no more than is necessary.</p> <p>To provide a competitive level of fixed cash remuneration, reflecting the skills and experience required.</p>	<p>Paid monthly and reviewed annually.</p> <p>The rates for 2017 are unchanged:</p> <ul style="list-style-type: none"> Chief Executive - £1,000,000 Chief Financial Officer - £800,000 <p>Further details on remuneration arrangements for the year ahead are set out in the annual report on remuneration.</p>	<p>Determined annually.</p> <p>Any future salary increases will be considered against peer companies and will not normally be greater than the average salary increase for RBS employees over the period of the policy. Other than in exceptional circumstances, the salary will not increase by more than 15% over the course of this policy.</p>
Fixed share allowance	To provide fixed pay that reflects the skills and experience required and responsibilities for the role. This will be delivered in shares subject to a retention period.	A fixed allowance paid entirely in shares. Individuals receive shares that vest immediately subject to any deductions required for tax purposes and a retention period will apply. Shares will be released from the retention period in equal tranches over a three year period. The fixed share allowance will broadly be paid in arrears, currently in two instalments per year. ⁽¹⁾ The fixed share allowance is not pensionable.	An award of shares with an annual value of up to 100% of salary at the time of award, or such higher amount which represents such value rounded up to the nearest whole share.
Benefits	To provide a range of flexible and market competitive benefits that are valued and assist key individuals in carrying out their duties effectively.	<p>A set level of funding is provided and executive directors can select from a range of standard benefits including, but not limited to:</p> <ul style="list-style-type: none"> company car private medical cover life assurance critical illness insurance <p>In addition, executive directors are entitled to travel assistance in connection with company business including the use of a car and driver. RBS will meet the cost of any tax due on the benefit. On rare occasions where they are accompanied by their spouse / partner to business events, RBS may also meet the costs and any associated tax liability. Executive directors are also entitled to holiday and sick pay.</p> <p>Further benefits including, but not limited to, relocation costs (e.g. tax advice, shipment and storage facilities, housing and flight allowances and payment of legal fees) may be offered in line with market practice. RBS may also put in place certain security arrangements for executive directors where that is deemed appropriate.</p>	<p>Set level of funding for standard benefits (currently £26,250) which is subject to review.</p> <p>The total value of benefits provided is disclosed each year in the annual report on remuneration.</p> <p>The maximum potential value of benefits will depend on the type of benefit and cost of its provision, which will vary according to market rates.</p>
Pension	To encourage planning for retirement and long-term savings.	Provision of a monthly cash pension allowance based on a percentage of salary. Opportunity to use the cash to participate in a defined contribution pension scheme.	Pension allowance for current executive directors of 35% of salary.

Note:

(1) The company believes that delivery in shares is the most appropriate construct for a fixed allowance to executive directors, qualifying as fixed remuneration for regulatory requirements. If regulatory requirements emerge that prohibit allowances being delivered in shares, or deem that such allowances will not qualify as fixed remuneration, then RBS reserves the right to provide the value of the allowance in cash instead in order to comply with the requirements.

Directors' Remuneration Policy

Variable pay

Variable pay is intended to incentivise the delivery of sustainable long-term performance, with rewards aligned to shareholders' interests and adjusted for risk. The first awards under the new policy will be made in early 2018.

Element of pay	Purpose and link to strategy	Operation	Maximum potential value	Performance assessment
Variable pay award (long-term incentive)	<p>To support a culture where individuals are rewarded for the delivery of sustained, target performance, taking into account RBS's strategic objectives.</p> <p>Performance will include a range of financial and non-financial factors to encourage long-term value creation for shareholders.</p> <p>Delivery in shares with the ability to apply malus adjustments and clawback further supports longer-term alignment with shareholders' interests.</p>	<p>Any variable pay awarded will be delivered as a long-term incentive, paid in shares and subject to performance assessment and employment conditions.</p> <p>Awards will be subject to deferral, malus, clawback, post-vesting retention periods and any other terms as required by regulators.</p> <p>A one year pre-grant performance period will apply and awards will also be subject to a pre-vest performance assessment at the end of a three year period, with vesting taking place from years three to seven after grant.</p> <p>Awards are subject to malus prior to vesting and clawback post vesting. Clawback applies for seven years from the date of award, extended to ten years if events are under investigation at the end of the normal seven-year clawback period. The post-vesting retention period will be 12 months.</p> <p>The award will be delivered under the RBS 2014 Employee Share Plan, as approved by shareholders at the 2014 AGM.</p>	<p>The maximum award for current directors is 175% of salary for the Chief Executive and 200% of salary for the Chief Financial Officer, or such higher amount which represents such value rounded up to the nearest whole share.</p> <p>Awards are also subject to the regulatory requirement that limits variable pay to the level of fixed pay and can be valued in line with EBA rules, including any available discount for long-term deferral.</p> <p>The regulatory limit is currently higher than the level under the proposed new policy.</p> <p>Prior performance will be taken into account when determining the value of the award at the time of grant.</p> <p>The vesting level of the award can vary between 0% and 100% dependent on the assessment of performance.</p>	<p>Performance will be assessed in the areas of Finance, Risk & Operations, Customers and our People to determine whether the executive has achieved what would reasonably have been expected in the circumstances.</p> <p>The Committee will consider relevant factors (e.g. CET1 ratio under the Finance heading and others relating to progress in the areas of Risk & Operations, Customers and People objectives) that are relevant to RBS's strategic aims but will apply its judgement for the most part without reference to formulaic targets.</p> <p>Risk & Control and Stakeholder Perception underpins will apply which may lead to downwards adjustment.</p> <p>Performance will be assessed in the round. The majority of the performance variation is expected to take place under the pre-grant test, with the pre-vest assessment representing a final check that, taking all circumstances into account, overall performance has been satisfactory.</p> <p>The Committee has discretion to vary the performance factors in appropriate circumstances.</p> <p>Further details on the performance factors and assessment will be set out in the annual remuneration report for the relevant year.</p>

Notes to policy table

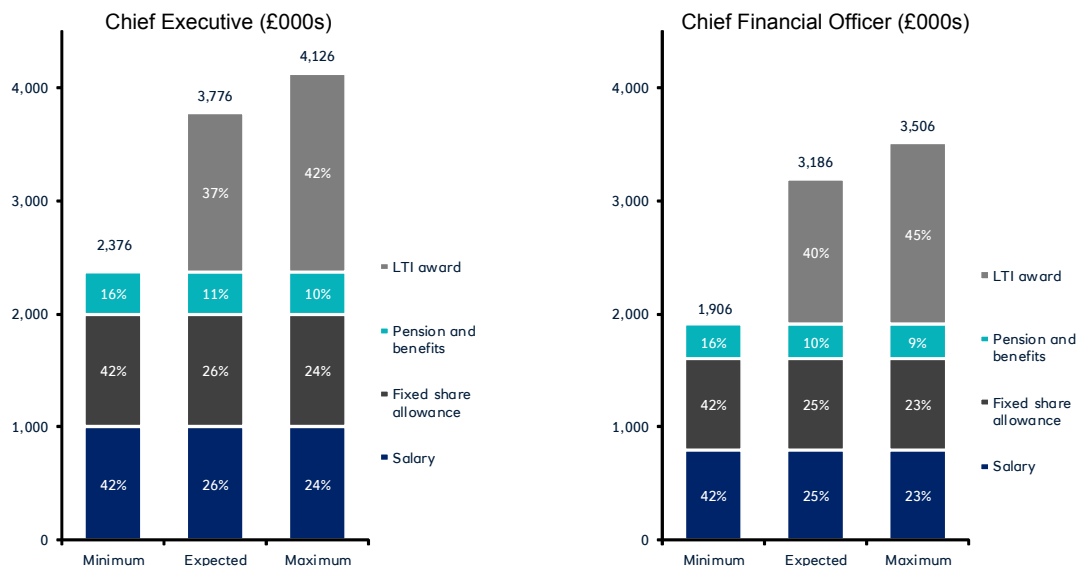
- The performance factors for variable pay awards have been chosen to reward sustained performance and are complemented by increased long-term shareholding requirements. Any targets will be set in line with RBS's strategic priorities.
- The fixed share allowance is part of fixed remuneration and is therefore not subject to any performance adjustment.
- Changes have been made under the proposed policy to lower the maximum quantum of LTI awards combined with performance factors considered to be more within the control of management and increased shareholding requirements. Further details on the changes can be found on page 89 to 92.
- Remuneration for executive directors broadly follows the policy for all employees but generally with a higher element of variable pay and greater delivery in shares, held for the long term to ensure appropriate alignment with the interests of shareholders.
- Further details on the remuneration policy for all employees, including details on how malus and clawback can be applied, can be found on pages 109 to 110.

Directors' Remuneration Policy

Other pay elements

Element of pay	Purpose and link to strategy	Operation	Maximum potential value
Shareholding requirements	To ensure executive directors build and continue to hold a significant shareholding to align with the interests of shareholders.	Executive directors are required to build up a shareholding equivalent to a percentage of salary. Unvested shares from LTI awards will count on a net of tax basis towards meeting the shareholding requirement once the pre-vest performance assessment has taken place, at the end of the three year period. Once the respective retention periods have passed, directors are permitted to dispose of up to 25% of the net of tax shares received until the shareholding requirement is met. Any shares purchased voluntarily will be excluded from this sale restriction.	Chief Executive 400% of salary Chief Financial Officer 250% of salary Requirements may be reviewed in future but are not expected to be reduced.
All-employee share plans	An opportunity to acquire RBS shares.	Opportunity to elect to contribute from salary and acquire shares under any of the company's all-employee share plans in operation from time to time, such as the RBS Sharesave and Buy As You Earn Plan. These plans are not subject to performance conditions.	Statutory limits imposed by HMRC or the applicable limits under the relevant plans.
Legacy arrangements	To ensure RBS can continue to honour payments due to executive directors.	In approving this policy, authority is given to honour any previous commitments or arrangements entered into with current or former directors, including share awards granted under the 2014 Employee Share Plan. LTI awards under the existing policy will normally vest over a three to seven year period subject to the achievement of relevant performance conditions, based on Economic Profit, Relative Total Shareholder Return, Safe & Secure Bank and Customers & People measures. Six month post-vesting retention periods and service requirements also apply. Further details of the value and terms of the awards can be found in the annual remuneration reports for the relevant years. Authority is also given to honour arrangements agreed for an employee prior to appointment as an executive director that may have different terms or performance conditions.	In line with existing commitments and arrangements.

Remuneration scenarios for current executive directors under the new remuneration policy



Notes:

- The charts above are for illustration only and do not take into account any share price movement over the period.
- The benefits figure includes standard benefit funding as outlined in the policy but excludes exceptional or business related items such as relocation allowances and travel assistance in connection with company business, the value of which will be disclosed in the total remuneration table each year.
- Subject to the performance assessment, LTI awards will vest between years three to seven from award and be subject to a 12 month retention period post vesting.
- The total maximum opportunity represents a 20% reduction for the Chief Executive and a 17% reduction for the Chief Financial Officer from that available under the current policy. The variable pay element is approximately 40% lower for the Chief Executive and 30% lower for the Chief Financial Officer than the current policy.
- The relatively minor difference between expected and maximum shown above is the consequence of a deliberate move to a less leveraged remuneration construct. The expected value has been calculated at 80% of maximum. The policy has a strong focus on long-term shareholding to create alignment with shareholders along with LTI awards assessed on factors that executive directors would reasonably be expected to achieve, encouraging performance within risk appetite.

Directors' Remuneration Policy

Remuneration for the Chairman and non-executive directors

Element of pay	Purpose and link to strategy	Operation	Maximum potential value
Fees	To provide a competitive level of fixed remuneration that reflects the skills, experience and time commitment required for the role.	<p>Fees are paid monthly in cash. The Board retains discretion to pay fees in shares as well as cash.</p> <p>The level of remuneration reflects the responsibility and time commitment required and the level of fees paid to directors of comparable major UK companies.</p> <p>Fees are reviewed regularly. Additional fees may be paid for new Board Committees provided these are not greater than fees payable for the existing Board Committees as detailed in the annual report on remuneration.</p> <p>No variable pay is provided so that the Chairman and non-executive directors can maintain appropriate independence, focus on long-term decision making and constructively challenge performance of the executive directors.</p>	<p>Following a review of the size of the Board against comparable companies and the relative time commitment for individual non-executive directors at RBS, it is proposed to increase the basic Board fee for non-executive directors in 2017 from the date of the AGM. This would be the first change in the basic Board fee since the policy was last approved in 2014. There is no change at this time to the Chairman's composite fee.</p> <p>The rates for the year ahead are set out in the annual report on remuneration.</p> <p>Any future increases to fees will be considered against fees paid to directors of comparable companies and will not normally be greater than the average inflation rate over the period under review, taking into account that any change in responsibilities, role or time commitment may merit a larger increase. Other than in exceptional circumstances, fees will not increase by more than 15% over the course of this policy.</p>
Benefits	To provide a level of benefits in line with market practice.	<p>Reimbursement of reasonable out-of-pocket expenses incurred in connection with the performance of duties.</p> <p>The Chairman and non-executive directors are entitled to travel assistance in connection with company business including the use of a car and driver. RBS will meet the cost of any tax due on the benefit. On rare occasions where they are accompanied by their spouse / partner to business events, RBS may also meet the costs and any associated tax liability. Other benefits may be offered in line with market practice.</p> <p>The Chairman also receives private medical cover.</p>	<p>The value of the private medical cover provided to the Chairman and any other benefits will be in line with market rates and disclosed in the annual report on remuneration.</p>

Discretion

The Committee has certain discretionary powers under the company's employee share plan rules. For example, the Committee has discretion to determine whether an individual would qualify as a good leaver on departure and also to decide that awards held by good leavers should vest earlier than the normal vesting date. Such discretions would only be used to ensure a fair outcome for the director and for shareholders, taking into account the circumstances of departure, the performance of the director and the need for an orderly transition. If discretion is applied in these circumstances then it will be disclosed.

Further discretions include the ability to: treat LTI awards in a range of ways in the event of a change of control, including the ability for LTI awards to be exchanged for new awards; change any performance measures, targets, and to adjust such awards if major events occur (for example transaction and capital raisings); and make administrative changes to the plan rules. In addition, the Committee retains discretion to apply malus and clawback to LTI awards. When assessing performance, the Committee can also adjust the number of shares that are received under LTI awards through the application of underpins in appropriate circumstances.

The Committee also retains the discretion to make reasonable and proportionate changes to the Directors' Remuneration Policy in order to respond to changing legal or regulatory requirements or guidelines (including but not limited to any PRA or FCA revisions to their remuneration rules and the EBA remuneration guidelines). Where proposed changes are considered to be material, the Committee will consult with RBS's major shareholders.

Directors' Remuneration Policy

Recruitment remuneration policy

- RBS considers both internal and external candidates and assesses the skills and experience required for each role. Pay is generally set at no more than is required to attract the most suitable candidate for the role;
- The policy on the recruitment of new directors aims to be competitive and to structure pay in line with the framework applicable to current directors, based on the elements of pay detailed in the policy table, recognising that some adjustment to quantum within that framework may be necessary to secure the preferred candidate;
- The pension allowance for new executive directors will be reduced from 35% to 25% of salary, to bring the rate more in line with that of other employees, with a corresponding increase to other elements of fixed pay;
- Consideration will be given to the skills and experience held by the individual being recruited, as well as the incumbent's position;
- In the event of an internal promotion, existing contractual commitments can continue to be honoured;
- A buy-out policy exists to replace awards forfeited or payments foregone. The buy-out policy is in line with regulatory requirements, including the PRA rules that apply to buy-outs concluded on or after 1 January 2017;
- The Committee will minimise buy-outs wherever possible and ensure they are no more generous than, and on substantially similar terms to, the original awards or payments they are replacing. No sign-on awards or other payments will be offered on joining;
- Any awards granted following the recruitment of a candidate may be made under the company's employee share plans from time to time or under the relevant provisions in the Listing Rules and will need to comply with regulatory requirements. Full details will be disclosed in the next remuneration report following recruitment; and
- The maximum level of variable pay which may be granted to new executive directors will be guided by, but not limited to, arrangements for existing executive directors and in any event will not be more than one times the level of fixed pay, valued according to EBA rules. The maximum level excludes any buy-out arrangements.

Other directorships

Agreement from the Board must be sought before directors accept any additional roles outside of RBS. Procedures are in place to make sure that regulatory limits on the number of directorships held are complied with. The Board would also consider whether it was appropriate for executive directors to retain any remuneration receivable in respect of any external directorships, taking into account the nature of the appointment. Neither of the current executive directors holds a non-executive director role at any other company at this time. Details of the directorships held by other directors can be found in the biographies section of the corporate governance report.

Consideration of employment conditions elsewhere in the company

The Committee retains oversight of the remuneration policy for all employees to ensure there is a fair and consistent approach throughout the organisation. The policy uses deferral, malus and clawback to promote effective risk management and alignment with shareholders' interests.

Consultation on remuneration generally takes place with our social partners, including representatives from UNITE. RBS is a fully accredited Living Wage employer and we set our minimum pay (including benefit funding) above the level that is required to meet this.

An annual employee opinion survey takes place which includes a number of questions on pay and culture. This includes questions on employees' understanding of how pay is determined and whether employees believe they are paid fairly for the work they do.

While employees are not directly consulted on the directors' remuneration policy, around 24,000 of our employees are shareholders through the company's employee share plans and have the ability to express their views through voting on the Directors' Remuneration Report.

Consideration of shareholders' views

An extensive consultation is undertaken every year with major shareholders, including UKFI and other stakeholders, on our proposed remuneration approach. The consultation process typically involves inviting our largest shareholders to attend either one-to-one meetings or roundtable discussions.

A range of topics are discussed including the remuneration policy for the year ahead and any significant changes. The process takes place in sufficient time for shareholders' views to be considered prior to the Committee making any final decisions on remuneration and variable pay awards.

In late 2016, meetings took place involving a number of institutional shareholders and shareholder bodies representing a substantial portion of the non-UKFI shareholding. The reaction to the consultation process was positive and allowed the Committee to gain valuable insight into any areas of concern. Shareholders and other stakeholders indicated they were supportive of the new remuneration construct, highlighting the reduction in maximum potential variable pay and increased shareholding requirements as favourable features.

Shareholders asked wide-ranging questions including how the performance tests would work and the rationale for removing pro rating for good leavers. The Committee Chairman explained how the expected value of pay would be broadly maintained over time under the new policy, provided that pro rating for good leavers did not apply, and that there were merits in assessing executive directors against factors considered to be more within their control and which they could reasonably be expected to achieve.

Shareholders continue to play a vital role in developing remuneration practices that support the long-term interests of the business and the Committee is grateful and greatly encouraged by their involvement in the process.

Directors' Remuneration Policy

Service contracts and policy on payments for loss of office – directors

Provision	Policy details for executive directors
Notice period	RBS or the executive director is required to give 12 months' notice to the other party to terminate the executive director's employment.
Payments for loss of office	There are no pre-determined provisions for compensation on termination. There is discretion for RBS to make a payment in lieu of notice (based on salary only) which is released in monthly instalments. The executive director must take all reasonable steps to find alternative work and any remaining instalments will be reduced as appropriate to offset income from any such work.
Treatment of outstanding employee share plan awards on termination	<p>Any shares awarded under the fixed share allowance and LTI awards will be treated in accordance with the relevant plan rules as approved by shareholders.</p> <p>Fixed share allowances Shares will continue to be released over the applicable retention period helping to ensure that former executive directors maintain an appropriate interest in RBS shares. In all leaver circumstances, executive directors will continue to be eligible to receive a pro-rated fixed share allowance to reflect the period up to the termination date.</p> <p>LTI awards made under the existing remuneration policy (approved at the 2014 AGM) LTI awards normally lapse on leaving unless the termination is for one of a limited number of specified 'good leaver' reasons or the Committee exercises its discretion to prevent lapsing. LTI awards held by good leavers will continue to be subject to pro rating, to reflect the proportion of the performance period that has elapsed at the date of termination, unless the Committee exercises its discretion to determine otherwise. LTI awards held by good leavers will normally vest on the original vesting dates, subject to the performance conditions being met.</p> <p>Changes for LTI awards made under the new remuneration policy Under the policy being proposed to the 2017 AGM, LTI awards made in future will not be subject to pro rating for time in good leaver circumstances, for the reasons outlined earlier in this report. Awards will also generally be made to good leavers in respect of the final year of employment.</p> <p>Good leaver definition for LTI awards This definition applies to all LTI awards that the executive director holds. Individuals will qualify for good leaver treatment if they leave due to ill-health, injury, disability, death, retirement, redundancy, the employing company ceasing to be a member of the Group, transfer of the employing business, or any other reason if and to the extent the Committee decides in any particular case.</p> <p>With respect to the 'retirement' category above, and recognising the typical length of tenure for executive director roles, retirement good leaver treatment for executive directors will typically be considered taking all circumstances into account. Factors the Committee would expect to be present before agreeing to good leaver treatment under retirement include: whether the individual has been in role for at least five years, or otherwise qualifies for retirement criteria under RBS's policy, has demonstrated satisfactory performance, is not leaving to work in a capacity considered to be competing directly and materially with RBS, and is leaving at a time and in a manner that is agreed with the Board.</p>
Other provisions	Contracts include standard clauses covering remuneration arrangements and discretionary incentive plans (as set out in this report), reimbursement of reasonable out-of-pocket expenses incurred in performance of duties, redundancy terms and sickness absence, the performance review process, the disciplinary procedure and terms for dismissal in the event of personal underperformance or breaches of RBS policies. The Committee retains the discretion to make payments (including but not limited to professional and outplacement fees) to facilitate smooth handovers, mitigate against legal claims and/or procure reasonable assistance with investigations or claims, subject to any payments being made pursuant to a settlement or release agreement.

Provision	Policy details for the Chairman and non-executive directors
Notice and termination provisions	The Chairman and the non-executive directors have letters of appointment reflecting their responsibilities and time commitments. They do not have notice periods and no compensation would be paid to the Chairman or non-executive directors in the event of termination of appointment, other than standard payments payable for the period served up to the termination date.

Election or re-election of directors

In accordance with the provisions of the UK Corporate Governance Code, all directors of the company stand for election or re-election annually by shareholders at the company's AGM.

Annual report on remuneration

Annual report on remuneration

The sections audited by the company's auditors, Ernst and Young LLP, are as indicated.

Implementation of remuneration policy in 2017

Details of remuneration to be awarded in 2017 to executive directors are set out below. The long-term incentive (LTI) award is the grant due to be made in March 2017 for the 2016 performance year and the structure reflects the longer deferral period under PRA requirements. Subject to the performance conditions being met, vesting will take place between years four to seven (with 50% of any vesting in year four and 50% split over years five to seven). This will be the last LTI award under the current remuneration policy with any subsequent awards being made under the proposed new remuneration policy set out on page 94. The fixed share allowance for 2017 will be granted after the 2017 AGM and, subject to shareholder approval of the proposed policy, will be released over a three year retention period.

Executive directors' remuneration to be awarded in 2017

	Salary	Standard benefits	Pension 35% of salary	Fixed share allowance 100% of salary (1)	LTI award calculated in line with regulatory cap (2)
Chief Executive	£1,000,000	£26,250 (3)	£350,000	£1,000,000	£2,870,000
Chief Financial Officer	£800,000	£26,250	£280,000	£800,000	£2,305,000

Note:

- (1) Fixed share allowance will be payable broadly in arrears, currently in two instalments per year, and the shares will be released in equal tranches over a three year period.
- (2) The LTI that can be awarded in 2017 is limited to the level of fixed remuneration, taking into account the EBA discount rules for long-term deferral. The discount factor is a mechanism to take account of opportunity costs and inflation risk for the value being provided over time and can be applied if the deferral period is at least five years. By incorporating the current discount factor, LTI awards can be granted in March 2017 with a face value of approximately 121% of fixed remuneration. For example, the Chief Executive received fixed remuneration of £2,376,250 in 2016 (based on standard benefits only) which allows an LTI award to be made at £2,870,000. Performance measures and targets are set out on page 103.
- (3) Amount shown relates to standard benefit funding. Executive directors are also entitled to benefits in line with the stated policy including travel assistance and the Chief Executive is entitled to a flight allowance as part of his relocation arrangements. The value of benefits will be disclosed each year in the total remuneration table.

Chairman and non-executive directors' fees for 2017

The basic Board fee for non-executive directors has been unchanged since the current remuneration policy was approved by shareholders in 2014. During 2016, the Group's Nominations and Governance Committee considered how Board fees for non-executive directors compared to peer companies. RBS has a smaller number of Board members than most, meaning that the relative time commitment for individual non-executive directors is likely to be greater. Non-executive directors have also absorbed a number of incremental responsibilities arising out of matters considered to be unique to RBS. It is proposed that the basic Board fee is increased from £72,500 to £80,000 per annum and, subject to shareholder approval being obtained, the change will take effect from the date of the AGM. A summary of the proposed annual fees payable is set out below.

Chairman (composite fee)		£750,000
Non-executive director basic fee (for period pre AGM)		£72,500
Non-executive director basic fee (for period post AGM)		£80,000
Senior Independent Director		£30,000
Group Audit Committee (GAC), Group Performance and Remuneration Committee (RemCo),	Member	£30,000
Board Risk Committee (BRC) and Sustainable Banking Committee (SBC)	Chairman	£60,000
Board Oversight Committee (BOC) for GRG,	Member	£15,000
US Risk Committee	Chairman	£30,000
NatWest Markets (formerly CIB) advisory role		£30,000
Group Nominations and Governance Committee	Member	£15,000

The CIB BOC was disbanded at the end of February 2016. However, the Board agreed that Robert Gillespie, the former CIB BOC Chairman, should continue in an advisory role, supporting the NatWest Markets (formerly CIB) CEO and senior management team during a transitional period for the business for which he receives fees of £30,000 per annum.

Annual report on remuneration

Total remuneration paid to executive directors for 2016 (audited)

	Ross McEwan		Ewen Stevenson	
	2016 £000	2015 £000	2016 £000	2015 £000
Salary	1,000	1,000	800	800
Fixed share allowance (1)	1,000	1,000	800	800
Benefits (2)	113	149	26	26
Pension	350	350	280	280
Total fixed remuneration (3)	2,463	2,499	1,906	1,906
Annual bonus	n/a	n/a	n/a	n/a
Long-term incentive award (4)	1,030	993	—	—
Total remuneration	3,493	3,492	1,906	1,906

Notes:

- (1) The value of the fixed share allowance is based on 100% of salary and, as part of fixed remuneration, it is not subject to any performance conditions. It is delivered in shares and released over a retention period.
- (2) Includes standard benefit funding of £26,250 per annum with the remainder being travel assistance in connection with company business (£74,621) and relocation expenses (£11,801) provided to Ross McEwan. The 2015 benefits figure for Ross McEwan has been restated to include a value for travel assistance during that year.
- (3) The total fixed remuneration at £2,463,000 is higher than the £2,376,250 fixed remuneration in the implementation of policy section as the lower figure includes standard benefits only.
- (4) The 2016 value for Ross McEwan relates to an LTI award granted in 2014 that is due to vest in March 2017. The performance conditions ended on 31 December 2016 and have been assessed as set out below together with an estimate of the vesting value. The value for 2015 has been amended from the estimated value of £1,347,000 provided in the 2015 report to reflect the actual value on the vesting date in March 2016.

2014 LTI – final assessment of performance measures (audited)

An assessment of performance of each relevant element was provided by internal control functions and PwC assessed relative Total Shareholder Return (TSR) performance against a peer group of comparator banks.

Performance Measures (and weightings)	Performance for minimum vesting	Vesting at minimum	Performance for maximum (100%) vesting	Actual Performance	Vesting outcome	Weighted Vesting %
Economic Profit (25%)	(£1 billion)	25%	£0	(£0.4 billion)	82%	20%
Relative TSR (25%)	TSR at median	20%	TSR at upper quartile	18 th percentile ranking	0%	0%
Safe & Secure Bank (25% split across two measures)	Vesting between 0% - 100% qualified by Committee discretion CET1 ratio target: >=12% Cost:income ratio target: 59%			CET1 ratio: 13.4% Cost:income ratio of 61%	88%	22%
Customers & People (25% split across two measures)	Vesting between 0% - 100% qualified by Committee discretion Net Promoter Score target: Gap to number 1 of 8.7 Engagement Index (EI) target: EI within 3 points of Global Financial Services (GFS) norm			Gap to number 1 of 13.4 EI: 6 points behind GFS norm	0%	0%
Overall vesting outcome (1)						42%

Note:

- (1) The Economic Profit outcome was determined according to the vesting scale where target performance of (£0.77 billion) would result in 62.5% vesting.

The vesting within the Safe & Secure Bank and Customers & People categories has been qualified by Committee discretion, taking into account the margin by which targets have been missed or exceeded and any other relevant factors. The CET1 ratio target was exceeded and the cost:income ratio was deemed to have been substantially met, reflecting the significant progress from the 2013 base year of 69% and recognising the significant headwinds in the external environment since that time. This resulted in 100% and 75% vesting respectively for these elements and a combined vesting outcome under the Safe & Secure category of 88%.

On the Customers measure, whilst absolute performance on the customer position had improved over the period, the target on closing the gap had been missed and in the circumstances the Committee concluded performance was not sufficient in order to justify vesting. On the People measure, the Committee recognised that engagement scores had been impacted by a number of unforeseen factors and difficult decisions required by management during the year but again it was felt that the level of vesting for this element should be nil.

The Committee also received input from the BRC. In making its final judgement, the Committee considered the overall context of performance including a number of factors such as the Williams & Glyn transaction. The Committee believed such factors were already adequately reflected across the performance categories and that the overall vesting outcome above was fair and appropriate.

Annual report on remuneration

2014 LTI vesting amount included in the total remuneration table (audited)

Ross McEwan was granted an LTI award in March 2014. The performance conditions as set out on the previous page ended on 31 December 2016 and the award is due to vest in March 2017. The average share price over the last three months of the financial year has been used to estimate the vesting value.

Ross McEwan				
Performance category	% vesting	Maximum RBS shares (1)	Vested RBS shares	Value (2)
Economic Profit	82%	305,064	244,052	
Relative TSR	0%	305,064	—	
Safe & Secure Bank	88%	305,064	268,457	
Customers & People	0%	305,064	—	
Overall vesting outcome based on above	42%		512,509	£1,030,143
<i>Maximum capped shares available to vest</i>			915,193	

Notes:

- (1) The maximum number of shares is calculated in line with the underlying award structure where each of the four performance categories could give rise to shares worth 100% of salary at grant but with the overall maximum capped at 300% of salary at grant. The percentage vesting under the Economic Profit category has been rounded from 82% to 80% when calculating the number of vested shares in order to maintain the overall weighted vesting outcome at 42%.
- (2) Based on a RBS share price of £2.01, the average over the three month period from October to December 2016.

2015 and 2016 LTI awards to executive directors – current assessment (audited)

The table represents an early indication of potential vesting outcomes only based on the position at 31 December 2016. Subject to the assessment of performance conditions over a three year period, these LTI awards will vest in years four and five from the date of grant. Details of the final performance assessment and any use of discretion will be disclosed in the remuneration report for the relevant year.

Performance measure	Weighting	Performance for minimum vesting	Vesting at minimum	Performance for maximum vesting	Vesting at maximum	2015 current assessment	2016 current assessment
Economic Profit	25%	Minimum economic profit targets	25%	Performance ahead of the Strategic Plan	100%	Good progress and currently favourable to target set	Currently tracking behind target range
Relative TSR	25%	TSR at median of comparator group	20%	TSR at upper quartile of comparator group	100%	Below median performance for vesting	Below median performance for vesting
Safe & Secure Bank	25%	Target ranges set for: CET1 ratio and Cost:income ratio	Vesting between 0% – 100% qualified by Committee discretion taking into account the margin by which targets have been missed or exceeded			CET1 ratio is in range for vesting. Cost:income ratio is broadly in line with target	CET1 ratio is in range for vesting. Cost:income ratio currently tracking behind target range
Customers & People	25%	Target ranges set for: Net Promoter Score, Net Trust Score and Employee Engagement				Customer & People measures currently tracking behind target range	Customer & People measures currently tracking behind target range

LTI awards granted during 2016 (audited)

	Grant date	Face value of award (£000s)	Number of shares awarded (1)	% vesting at minimum and maximum	Performance Requirements (2)
Ross McEwan	8 March 2016	2,680	1,187,207	Between 0% - 100% with minimum vesting as set out above	Conditional share awards subject to performance conditions, as set out above, measured over the three year period from 1 January 2016 to 31 December 2018
Ewen Stevenson	8 March 2016	2,150	952,424		

Notes:

- (1) The number of shares awarded was calculated in line with the regulatory cap that limits variable pay to the level of fixed pay and for this award equated to 268% of salary. The award price of £2.2574 was calculated based on the average share price over five business days prior to the grant date.
- (2) The awards are eligible to vest in equal tranches in 2020 and 2021, subject to the achievement of performance conditions. Malus provisions will apply up until vesting and clawback provisions will also apply for a period of seven years from the date of grant.

Annual report on remuneration

Performance conditions for LTI awards to be granted to executive directors in 2017, for the 2016 performance year

This will be the last LTI award under the current remuneration policy, with any subsequent awards being made under the new remuneration policy, subject to shareholder approval at the 2017 AGM. A three year performance period will apply until 31 December 2019. Subject to the achievement of the performance conditions, shares will vest 50% four years from the date of grant with the remaining 50% vesting pro rata between years five to seven from grant. Any awards that vest will be subject to a six month retention period.

Awards granted to executive directors in March 2017 will be subject to four equally weighted performance categories, each able to vest up to 100% of base salary, subject to the maximum award that is possible under the policy and the regulatory cap. Details of the performance measures and the Committee's rationale for selecting them are set out below.

Economic Profit (25%)

Reason: Economic Profit, being a risk-adjusted financial measure, is consistent with regulatory requirements and provides a balance between measuring growth and the cost of capital employed in delivering that growth.

Measure: Economic Profit for RBS defined as profit after tax less preference share charges less tangible net asset value multiplied by the cost of equity.

Performance target and weightings

Weighting	Performance target	Vesting range
25%	Target consistent with the achievement of RBS's strategic long term return on equity target	25% - 100%

Relative Total Shareholder Return (25%)

Reason: Relative TSR provides a direct connection between executive directors' awards and relative returns delivered to shareholders.

Measure: The measure compares performance against a group of comparator banks. The TSR comparator group was updated for awards made in 2016 to more accurately reflect the business strategy with reduced focus on investment banking. No changes have been made for the awards to be granted in March 2017.

Relative TSR Comparator Group

	Weighting
1 Barclays	200%
2 Lloyds Banking Group	100%
3 HSBC	50%
4 to 13 BBVA, BNP Paribas, Credit Agricole, ING, Intesa San Paolo, Nordea, Santander, Societe Generale, Standard Chartered, Unicredit	

Performance target and weightings

Weighting	Performance target	Vesting range
25%	TSR between median and upper quartile	20% - 100%

Safe & Secure Bank (25%)

Reason: The Safe & Secure Bank measures have a particular focus on risk reduction and the building of a safe, sustainable business.

Measure: The key measures in this category are the achievement of pre-determined Common Equity Tier 1 (CET1) and Cost:income (C:I) ratios.

Performance target and weightings

Category	Metrics and weighting	Performance target
Safe & Secure Bank	CET1 ratio (12.5%)	CET1 ratio target of $\geq 13\%$
	C:I ratio (12.5%)	C:I ratio target of 56%

Customers & People (25%)

Reason: These measures reward management for building a customer-focused business with engaged employees.

Measure: Net Promoter Scores (NPS) and Net Trust Scores (NTS) will be used. Employee engagement will be measured against the Global Financial Services (GFS) norm.

Performance target and weightings

Category	Metrics and weighting	Performance target
Customers & People	Advocacy (7.5%)	Significant progress on NPS and NTS scores
	Trust (5%)	
	Engagement (12.5%)	Employee Engagement Index one point above GFS norm

The overall vesting under the Safe & Secure Bank and Customers & People categories will be qualified by the Committee's discretion taking into account changes in circumstances over the performance period, the margin by which individual targets have been missed or exceeded, and any other relevant factors.

In line with previous practice, the Economic Profit is considered to be commercially sensitive. Within the Customers category, new metrics are being developed which will target trust and advocacy, specific to customers on a segmental basis, and will be consistent with RBS's long-term ambition. Further information on the trust and advocacy targets will be disclosed in the 2017 Directors' Remuneration Report, to the extent permitted by commercial sensitivity. Details of all targets and performance against these will be disclosed retrospectively after any vesting has been determined, in the annual report on remuneration for 2019.

Underpin

The Committee will also review financial and operational performance against the business strategy and the risk environment prior to agreeing vesting of awards. In assessing the risk considerations, the Committee will be advised independently by the BRC. If the Committee considers that the vesting outcome calibrated in line with the performance conditions outlined above does not reflect underlying financial results, or if the Committee is not satisfied that conduct and risk management during the performance period has been effective, then the terms of the awards allow for an underpin to be used to reduce vesting or lapse the award.

Annual report on remuneration

Payments for loss of office (audited)

No remuneration payment or payment for loss of office was made to directors during 2016.

Payments to past directors (audited)

Stephen Hester and Bruce Van Saun received shares in March 2016 on the vesting of the LTI award granted in 2013 as set out below.

The assessment of RBS-wide performance measures is detailed on page 73 of the 2015 Annual Report and Accounts.

Value of payments on vesting (audited)

Performance category	% vesting	Stephen Hester			Bruce Van Saun		
		Maximum RBS shares (2)	Vested RBS shares	Value (3)	Maximum CFG shares (2)	Vested CFG shares	Value (3)
Economic Profit	62%	107,805	66,839		65,656	40,706	
Relative TSR	0%	107,805	0		65,656	0	
Balance Sheet & Risk	90%	107,805	97,025		65,656	59,090	
Strategic Scorecard	72%	107,805	77,620		65,656	47,272	
Initial vesting outcome based on above	56%		241,484			147,068	
Final outcome post application of underpin (1)	50%		215,718	£496,799		131,377	\$2,828,547
<i>Maximum capped number of shares available to vest</i>			<i>323,415</i>			<i>196,967</i>	

Notes:

- (1) The Committee also considered recommendations from the BRC and concluded it would be appropriate to apply the risk and financial performance underpin in respect of the above awards. This resulted in downward discretion being applied to reduce the final vesting outcome from 56% to 50%.
- (2) The maximum number of shares is calculated in line with the underlying award structure where each of the four performance categories could give rise to shares worth 100% of salary at grant but with the overall maximum capped at 300% of salary. The number has been reduced on a pro rata basis to reflect time served by Stephen Hester. The interests for Bruce Van Saun's award were converted to shares in Citizens Financial Group, Inc. as part of the IPO of that business.
- (3) Based on a RBS share price of £2.303 and Citizens Financial Group, Inc. share price of \$21.53 on the date of vesting.

Total remuneration paid to the Chairman and non-executive directors for 2016 (audited)

A new Group Nominations and Governance Committee was established at the end of January 2016, replacing the former Group Nominations Committee, with an expanded remit and a reduced number of members. The RCR BOC and CIB BOC were stood down at the end of January and February 2016 respectively. The US steering group was stood down in 2016 and a new US Risk Committee was established to comply with US Enhanced Prudential Standards and the first meeting took place in May 2016. The total fees paid during 2016 are set out below.

Chairman (composite fee)	Fees	Fees	Benefits	Benefits	Total	Total
	2016 £000	2015 £000	2016 £000	2015 £000	2016 £000	2015 £000
Howard Davies (1)	750	260	8	2	758	262

Non-executive directors (2)	Noms & Gov										Fees	Fees	Benefits	Benefits	Total	Total
	Board £000	Gov £000	GAC £000	RemCo £000	BRC £000	SBC £000	RCR BOC £000	CIB BOC £000	GRG BOC £000	Other £000	2016 £000	2015 £000	2016 £000	2015 £000	2016 £000	2015 £000
Sandy Crombie (3)	73	14	30	60			1		15	30	223	227	—	—	223	227
Frank Dangeard (4)	46				12						58	—	—	—	58	—
Alison Davis	73	14		30		30					147	143	—	—	147	143
Morten Friis (3)	73		30		30			3		23	159	169	—	—	159	169
Robert Gillespie (3)	73	14		30	18	30		5	15	25	210	305	—	—	210	305
Penny Hughes	73				30	60					178	182	—	—	178	182
Brendan Nelson	73	14	60		30		1	3	30		211	217	—	—	211	217
Baroness Noakes (3)	73		30		60		2	3	15	9	192	223	—	—	192	223
Mike Rogers (4)	68					20					88	—	—	—	88	—

Notes:

- (1) Howard Davies joined the Board on 14 July 2015 and became Chairman with effect from 1 September 2015. The Benefits column includes private medical cover.
- (2) In line with market practice, non-executive directors are reimbursed expenses incurred in connection with their attendance at Board meetings. To the extent that HMRC determines that any amounts are taxable, RBS will settle the associated tax liability on behalf of the non-executive director.
- (3) Under the 'Other' column, Sandy Crombie received fees as the Senior Independent Director and Morten Friis received fees for his work on the US steering group until April 2016. The US Risk Committee was established with Morten Friis and Baroness Noakes receiving fees as Chairman and member of the Committee respectively. Robert Gillespie received fees for his role as an advisor to the NatWest Markets (formerly CIB) CEO and senior management.
- (4) Frank Dangeard and Mike Rogers joined the Board on 16 May 2016 and 26 January 2016 respectively.

Key to table:

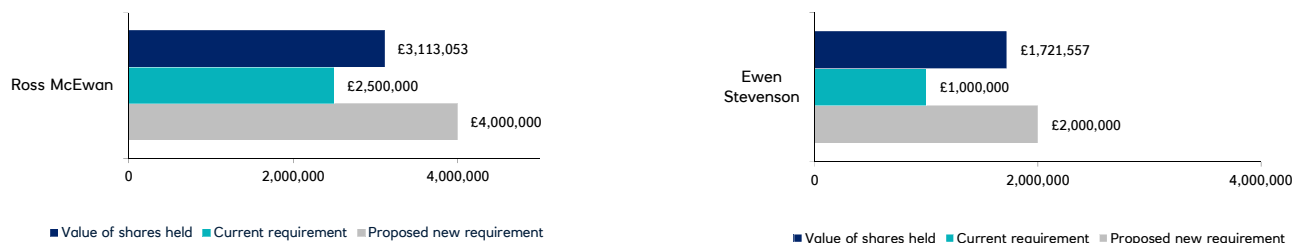
Noms & Gov	Group Nominations and Governance Committee
GAC	Group Audit Committee
RemCo	Group Performance and Remuneration Committee
BRC	Board Risk Committee
SBC	Sustainable Banking Committee
BOC	Board Oversight Committee for the RCR, NatWest Markets (formerly CIB) and GRG business areas

Annual report on remuneration

Directors' interests in shares and shareholding requirements (audited)

The current shareholding requirement is to hold shares to the value of 250% of salary for the Chief Executive and 125% of salary for the Chief Financial Officer. Under the proposed new policy, the requirement will be increased to 400% of salary for the Chief Executive and 250% of salary for the Chief Financial Officer, as detailed in the remuneration policy section of this report.

Shareholding requirements for executive directors



Notes:

- (1) Ross McEwan holds 259,455 shares from his 2015 and 2016 fixed share allowances that are included in the total shares beneficially owned below but these have been excluded from the shareholding requirements calculation as he will transfer these shares to charity at the end of the retention period.
- (2) Value of shares held is based on the share price of £2.246 as at 31 December 2016. During the year ended 31 December 2016, the share price ranged from £1.489 to £3.02.

Share interests held by directors

	Shares owned at 31 December 2016 (or date of cessation if earlier)	Unvested Long-term incentive awards
Ross McEwan	1,645,498	2,519,886
Ewen Stevenson	766,499	1,818,809
Howard Davies	41,000	
Sandy Crombie	20,000	
Frank Dangeard	—	
Alison Davis	20,000	
Morten Friis	20,000	
Robert Gillespie	25,000	
Penny Hughes	562	
Brendan Nelson	12,001	
Baroness Noakes	41,000	
Mike Rogers	—	

No other director had an interest in the company's ordinary shares during the year or held a non-beneficial interest in the shares of the company at 31 December 2016, at 1 January 2016 or date of appointment if later. The interests shown above include shares held by persons closely associated with the directors. As at 23 February 2017, there were no changes to the directors' interests in shares shown in the table above.

Directors' interests under the company's share plans (audited)

Long-term incentive awards

	Awards held at 1 January 2016	Awards granted in 2016	Award price £	Awards vested in 2016	Market price on vesting £	Value on vesting £	Awards lapsed in 2016	Awards held at 31 December 2016	Expected vesting date
Ross McEwan	696,152		3.09	431,614	2.30	992,712	264,538	—	
	915,193		3.28					915,193	07.03.17
	417,486		3.74					417,486	06.03.19 – 06.03.20
		1,187,207	2.26					1,187,207	08.03.20 – 08.03.21
	2,028,831	1,187,207		431,614			264,538	2,519,886	
Ewen Stevenson	435,611 (1)		3.27	147,354	2.30	338,914		288,257	07.03.17
	578,128		3.74					578,128	06.03.19 – 06.03.20
		952,424	2.26					952,424	08.03.20 – 08.03.21
	1,013,739	952,424		147,354				1,818,809	

Deferred awards

	Awards held at 1 January 2016	Awards granted in 2016	Award price £	Awards vested in 2016	Market price on vesting £	Value on vesting £	Awards lapsed in 2016	Awards held at 31 December 2016	Expected vesting date
Ross McEwan	18,797		3.09	18,797	2.30	43,233		—	

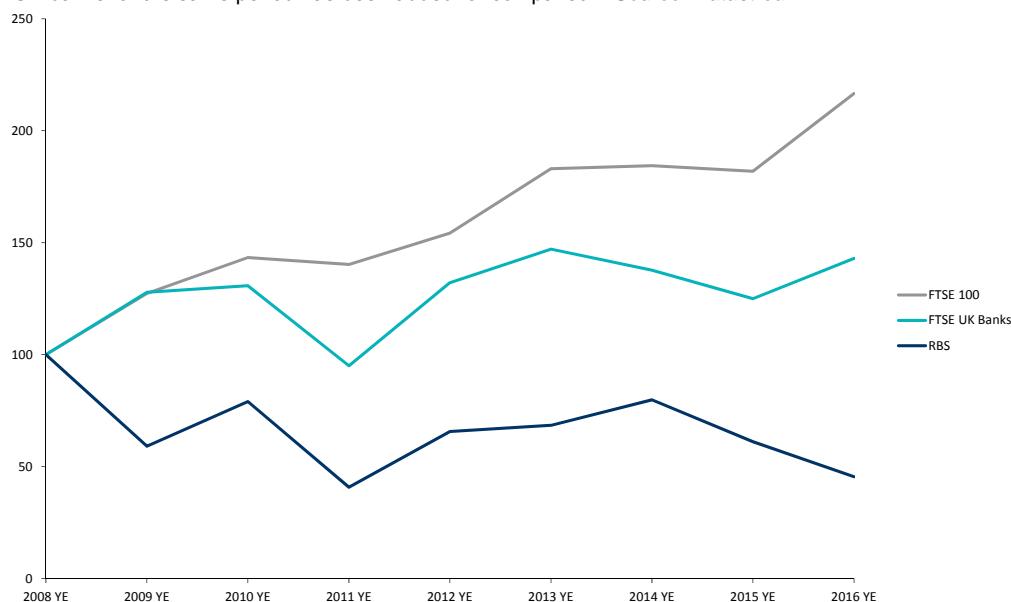
Note:

- (1) Award granted to Ewen Stevenson on appointment in May 2014 to replace awards forfeited on leaving Credit Suisse.

Annual report on remuneration

Total Shareholder Return (TSR) performance

The graph below shows the performance of RBS over the past eight years in terms of TSR compared with that of the companies comprising the FTSE 100 Index. This index has been selected because it represents a cross-section of leading UK companies. The TSR for FTSE UK banks for the same period has been added for comparison. *Source: Datastream*



Chief Executive pay over same period

	2009	2010	2011	2012	2013 (1)	2014	2015	2016
Total remuneration (£000s)					393 (RM)	1,878	3,492	3,493
Annual bonus against maximum opportunity	1,647	3,687	1,646	1,646	1,235 (SH)	n/a	n/a	n/a
LTI vesting rates against maximum opportunity	0%	85%	0%	0%	0%	72.85%	62%	56%

Notes:

- (1) 2013 remuneration includes Stephen Hester (SH) as CEO for the period to 30 September and Ross McEwan (RM) for the period from 1 October to 31 December 2013.
 (2) Figures have been amended where appropriate to reflect any restatement of prior year amounts, for example, to reflect the actual rather than estimated value of LTI vestings as part of the total remuneration figure and any revisions to the value of benefits provided.

Change in Chief Executive pay compared with employees

The table below shows the percentage change in remuneration for the Chief Executive between 2015 and 2016 compared with the percentage change in the average remuneration of RBS employees based in the UK. In each case, remuneration is based on salary, benefits and annual bonus.

	Salary 2015 to 2016 change	Benefits 2015 to 2016 change	Annual Bonus 2015 to 2016 change
Chief Executive (1)	0%	0%	n/a
UK employees (2)	4.51%	4.18%	(4.86%)

Notes:

- (1) Executive directors are not eligible for an annual bonus. Standard benefit funding for executive directors remained unchanged between 2015 and 2016. The benefits for the Chief Executive excludes other benefits such as travel assistance in connection with company business and relocation benefits, the value of which is disclosed each year in the total remuneration table. In 2016, Ross McEwan also received a fixed share allowance as part of his fixed pay.
 (2) The size of the percentage increase for fixed pay elements to 2016 is partly due to the one-off impact of removing incentives for certain frontline roles. The data represents full year salary costs of the UK based employee population, which covers the majority of RBS employees and is considered to be the most representative comparator group.

Annual report on remuneration

Relative importance of spend on pay

The table below shows a comparison of remuneration expenditure against other distributions and charges.

	2016 £m	2015 (1) £m	change
Remuneration paid to all employees (2)	4,670	5,208	(10.3%)
Distributions to holders of ordinary shares	—	—	
Distributions to holders of preference shares and paid-in equity (3)	1,697	385	341%
Taxation and other charges recognised in the income statement:			
- Social security, Bank levy and Corporation tax	747	597	25.1%
- Irrecoverable VAT and other indirect taxes incurred by RBS (4)	697	691	0.9%

Notes:

(1) Numbers exclude discontinued operations, principally CFG in 2015.

(2) Remuneration paid to all employees represents total staff expenses per Note 3 to the Financial Statements, exclusive of social security and other staff costs.

(3) Includes final payment relating to the Dividend Access Share of £1,193 million in 2016.

(4) Input VAT and other indirect taxes not recoverable by RBS due to it being partially exempt.

The items above have been included as they reflect the key stakeholders for RBS and the major categories of distributions and charges made by RBS.

Consideration of matters relating to directors' remuneration

Membership of the Group Performance and Remuneration Committee

All members of the Committee are independent non-executive directors. The Committee held seven scheduled meetings in 2016 and a further two ad hoc meetings.

	Attended/ scheduled
Sandy Crombie (Chairman)	7/7
Alison Davis	7/7
Robert Gillespie	7/7

Mike Rogers was appointed as a new member of the Committee with effect from 1 January 2017.

The role and responsibilities of the Committee

The Committee is responsible for:

- approving the remuneration policy for all employees and reviewing the effectiveness of its implementation;
- reviewing performance and making recommendations to the Board on remuneration arrangements for executive directors;
- approving remuneration arrangements for members and formal attendees of the Executive Committee and employees with total annual compensation which exceeds an amount determined by the Committee, currently £1 million; and
- setting the remuneration framework and principles for employees identified as Material Risk Takers falling within the scope of UK regulatory requirements.

In mitigating potential conflicts of interest, directors are not involved in decisions regarding their own remuneration and remuneration advisers are appointed by the Committee rather than management. The terms of reference of the Committee are reviewed annually and available on rbs.com.

Summary of the principal activity of the Committee in 2016

The new executive director remuneration policy and any issues arising under the accountability review process were considered at the majority of meetings. Set out below is a summary of other key activities considered by the Committee.

First quarter

- 2015 performance reviews and remuneration arrangements for members and attendees of the Executive Committee and high earners.
- Approval of variable pay pools and the 2015 Directors' Remuneration Report.
- Assessment of the performance of LTI awards granted in prior years and performance targets for 2016 awards.
- Executive Committee members' 2016 objectives.

Second quarter

- Key external trends and regulatory updates.
- Annual review of external advisers to the Committee.
- Remuneration governance across legal entities and the impact of the Senior Managers Regime.
- Annual review of remuneration policy for all employees.

Third quarter

- 2016 half-year performance reviews for members and attendees of the Executive Committee and high earners.
- Considering the future pay construct for all employees.
- Interim business performance assessment.
- Divestment principles update.
- External stakeholder engagement plan.

Fourth quarter

- Review of the implementation of the remuneration policy.
- 2016 preliminary pay elements including bonus pool, deferral and LTI awards.
- Executive Committee members' annual objectives for 2017.
- Update on regulatory requirements.
- Stakeholder engagement and feedback on new remuneration policy for executive directors.
- Review of draft Directors' Remuneration Report for 2016.

Annual report on remuneration

Performance evaluation process

The Committee has considered the findings of the annual review of the effectiveness of the Committee which was conducted internally by the Chief Governance Officer and Board Counsel.

Positive comments were received on moving to a reduced number of meetings with appropriate use of delegation, giving time to focus on important issues such as the future pay construct. There was good evidence of challenge on key points of principle during debates and overall it was felt that the dynamic of the Committee worked well. The Masterclass sessions, where in-depth consideration is given to specific matters, continued to be well received by members.

On areas for development, the importance of papers containing all the relevant information was highlighted and there was still scope to further improve the articulation of how reward links to strategy. There was also a suggestion that it would be helpful for the Committee to have another member. Subsequently, the Board agreed that Mike Rogers would be appointed to the Committee with effect from 1 January 2017.

Potential areas were identified for future focus by the Committee including absolute pay levels, competitiveness and internal fairness.

Advisers to the Committee

The Committee reviews its selection of advisers annually. PricewaterhouseCoopers LLP (PwC) was appointed as the Committee's remuneration advisers on 14 September 2010 following a review of potential advisers, and the appointment was reconfirmed by the Committee in May 2016 after an annual review of the quality of the advice received and fees charged. PwC is a signatory to the voluntary code of conduct in relation to remuneration consulting in the UK.

PwC also provide professional services in the ordinary course of business including assurance, advisory, tax and legal advice to RBS subsidiaries. There are processes in place to ensure the advice received by the Committee is independent of any support provided to management. As well as receiving advice from PwC in 2016, the Committee took account at meetings of the views of the Chairman; Chief Executive; Chief Financial Officer; Chief HR Officer; the Director of Organisation and Performance; the Chief Governance Officer and Board Counsel; the Chief Risk Officer; and the Chief Conduct and Regulatory Affairs Officer. The fees paid to PwC for advising the Committee in relation to directors' remuneration are charged on a time/cost basis and in 2016 amounted to £214,706 excluding VAT (2015 - £121,358). The increase in fees is a result of additional work undertaken during 2016 in developing the new directors' remuneration policy.

Statement of shareholding voting

The tables below set out the voting by shareholders on the resolution to approve the Annual Report on Remuneration at the AGM held in May 2016 and the resolution at the AGM in June 2014 when the Directors' Remuneration Policy was last approved.

Annual Report on Remuneration – 2016 AGM

For	Against	Total votes cast	Withheld
42,686,046,288 (99.56%)	188,029,796 (0.44%)	42,874,076,084	6,603,412

Directors' Remuneration Policy – 2014 AGM

For	Against	Total votes cast	Withheld
20,893,215,888 (99.66%)	70,382,756 (0.34%)	20,963,598,644	170,307,216

Shareholder dilution

During the ten year period to 31 December 2016, awards made that could require new issue shares to be used in connection with the company's employee share plans represented 5.4% of the company's issued ordinary share capital, leaving an available dilution headroom of 4.6%. The company meets its employee share plan obligations through a combination of new issue shares and market purchase shares.

Sandy Crombie
Chairman of the Group Performance and Remuneration
Committee
23 February 2017

Other Remuneration Disclosures

Remuneration of eight highest paid senior executives below Board (1)

	Executive 1	Executive 2	Executive 3	Executive 4	Executive 5	Executive 6	Executive 7	Executive 8
	£000	£000	£000	£000	£000	£000	£000	£000
Fixed pay (cash)	800	800	675	688	588	638	575	450
Fixed allowances	800	800	675	688	588	638	288	225
Annual bonus	—	—	—	—	—	—	—	—
Long-term incentive awards (vested value)	175	175	412	261	167	—	250	—
Total remuneration (2)	1,775	1,775	1,762	1,637	1,343	1,276	1,113	675

Notes:

(1) Remuneration earned in 2016 for eight members of the Executive Committee.

(2) Disclosure includes prior year long-term incentive awards which vested during 2016. The amounts shown reflect the value of vested awards using the share price on the day the awards vested.

How risk is reflected in our remuneration process

The RBS remuneration policy explicitly aligns remuneration with effective risk management. Focus on risk is achieved through clear risk input into objectives, performance reviews, the determination of variable pay pools and incentive plan design as well as the application of malus and clawback. The Committee is supported in this by the BRC and the RBS Risk function.

A robust process is used to assess risk performance. A range of measures are considered, specifically the overall Risk Profile; Credit, Regulatory and Conduct Risk; Operational Risk; Enterprise Risk; and Market Risk. The steps we take to ensure appropriate and thorough risk adjustment are also fully disclosed and discussed with the PRA and the FCA.

Variable pay pool determination

For the 2016 performance year, RBS has operated a multi-step process which is a control function led assessment to determine performance and therefore the appropriate bonus pool by franchise and function.

The process considers a balanced scorecard of performance assessments at the level of each franchise or support function. The assessments are made across financial, customer and people measures. Risk and conduct assessments at the same franchise or functional level are then undertaken to ensure that performance achieved without the appropriate risk and conduct controls and culture is not inappropriately rewarded.

BRC will then review any material risk and conduct events and if appropriate an underpin may be applied to the individual business and function bonus pools and where appropriate to the overall RBS bonus pool. BRC may recommend reduction of a bonus pool if it considers that risk and conduct performance is unacceptable or that the impact of poor risk management has yet to be fully reflected in the respective inputs.

Following further review against overall performance and conduct, the Chief Executive will make a final recommendation to the Committee, informed by all the previous steps in the process and his strategic view of the business. The Committee will then make an independent decision on the final bonus pool taking all of these earlier steps into account.

Accountability review process and malus/clawback

An accountability review process is operated that allows RBS to respond in instances where new information would change the variable pay decisions made in previous years and/or the decisions to be made in the current year. Under the accountability review process, RBS can apply malus and clawback.

- Malus can be applied to reduce (if appropriate to zero) the amount of any variable pay awards prior to payment taking place.
- Clawback provisions can also be applied to recover awards that have vested.

Any variable pay awarded to Material Risk Takers from 1 January 2015 onwards is subject to clawback for seven years from the date of grant. For awards made in respect of the 2016 performance year onwards, this period has been extended to ten years for executive directors and other Senior Managers under the Senior Managers Regime where there are outstanding internal or regulatory investigations at the end of the normal seven-year clawback period. Malus and clawback can be applied to current and former employees.

There are a number of trigger events under which malus and clawback will be considered including:

- the individual participating in or being responsible for conduct which results in significant losses for RBS;
- the individual failing to meet appropriate standards of fitness and propriety;
- reasonable evidence of an individual's misbehaviour or material error;
- RBS or the individual's relevant business unit suffering a material failure of risk management; and
- in the case of malus only, circumstances where there has been a material downturn in financial performance.

How have we applied this in practice?

During 2016 a number of issues and events were considered under the accountability review framework. The outcomes covered a range of actions including: reduction and forfeiture of unvested awards through malus; reduction of current year variable pay awards; dismissal with forfeiture of unvested awards; and suspension of awards pending further investigation.

Other Remuneration Disclosures

Our remuneration policy for all employees

The remuneration policy supports the business strategy and is designed to promote the long-term success of RBS. It aims to reward employees for delivering good performance against targets provided this is achieved in a manner consistent with our values and within acceptable risk parameters. The remuneration policy applies the same principles to all employees including Material Risk Takers (MRTs) subject to UK regulatory requirements ⁽¹⁾. The current key elements underpinning the remuneration policy are set out below.

Element of pay	Objective	Operation
Base salary	To aid recruitment and retention of high performing individuals whilst paying no more than is necessary. To provide a competitive level of fixed cash remuneration, reflecting the skills and experience required, and to discourage excessive risk taking.	Base salaries are reviewed annually and should reflect the talents, skills and competencies that the individual brings to the business.
Role-based allowance	To provide fixed pay that reflects the skills and experience required for the role.	Allowances are provided to certain employees in key roles in line with market practice and qualify as fixed remuneration for regulatory requirements. They are delivered in cash and/or shares depending on the level of the allowance and the seniority of the recipient. Shares are subject to an appropriate retention period, not less than six months.
Benefits (including pension)	To provide a range of flexible and market competitive benefits. To encourage planning for retirement and long-term savings.	In most jurisdictions, employee benefits or a cash equivalent are provided from a flexible benefits account.
Annual bonus	To support a culture where employees recognise the importance of serving customers well and are rewarded for superior performance.	<p>The annual bonus pool is based on a balanced scorecard of measures including Customer, Financial, Risk and People measures. Allocation from the pool depends on performance of the franchise or function and the individual. Individual performance assessment is supported by a structured performance management framework.</p> <p>Immediate cash awards are limited to a maximum of £2,000. Under the deferral arrangements a significant proportion of annual bonus awards for our more senior employees are deferred over a three to seven year period. Awards are subject to malus and clawback provisions. For MRTs, a minimum of 50% of any annual bonus is delivered in shares and subject to a minimum six month retention period post vesting in line with regulatory requirements.</p> <p>Guaranteed awards are only used in very limited circumstances in accordance with regulatory requirements.</p>
Long-term incentive awards	To support a culture where good performance against a full range of measures will be rewarded. To encourage the creation of value over the long term and to align further the rewards of the participants with the returns to shareholders.	<p>RBS provides certain employees in senior roles with long-term incentive awards. Awards are structured as performance-vesting shares. Performance is typically measured over a three year period. For awards made in respect of the 2016 performance year, vesting will take place over a three to seven year period.</p> <p>The amount of the award that vests may vary between 0% -100% depending on the performance achieved. Awards are subject to malus and clawback provisions and a minimum six month retention period applies to MRTs post vesting.</p>
Other share plans	To offer employees in certain jurisdictions the opportunity to acquire shares.	Employees in certain countries are eligible to contribute to share plans which are not subject to performance conditions.

Note:

(1) The EBA has issued criteria for identifying MRT roles i.e. staff whose professional activities have a material influence over RBS's performance or risk profile. The criteria for identifying MRTs are both qualitative (based on the nature of the role) and quantitative (i.e. those who exceed the stipulated total remuneration threshold based on the previous year's total remuneration).

The qualitative criteria can be summarised as: staff within the management body; senior management; other staff with key functional or managerial responsibilities; staff, individually or as part of a Committee, with authority to approve new business products or to commit to credit risk exposures and market risk transactions above certain levels. The quantitative criteria are: individuals earning €500,000 or more in the previous year; individuals in the top 0.3% of earners in the previous year; individuals who earned more than the lowest paid identified staff per the qualitative criteria, subject to specific exceptions in the criteria.

In accordance with UK regulatory requirements and internal dealing rules that apply to employees, the conditions attached to discretionary share-based awards prohibit the use of any personal hedging strategies to lessen the impact of a reduction in value of such awards. These conditions are explicitly acknowledged and accepted by employees when any share-based awards are granted.

Other Remuneration Disclosures

Remuneration of MRTs

The quantitative disclosures below are made in accordance with Article 450 of the EU Capital Requirements Regulation in relation to 665 employees who have been identified as MRTs.

1. Aggregate remuneration expenditure

Aggregate remuneration expenditure in respect of 2016 performance was as follows:

PBB, CPB and NatWest Markets (formerly CIB)	Franchises £m	Rest of RBS £m	Total £m
	211.6	143.5	355.1

2. Amounts and form of fixed and variable remuneration

Fixed remuneration for 2016

Consisted of salaries, allowances, pensions and benefits.

	Senior management	Other MRTs	Total
Number of beneficiaries	11	654	665
	£m	£m	£m
Total fixed remuneration	17.4	205.7	223.1

Variable remuneration awarded for 2016 performance

Variable remuneration consisted of a combination of annual bonus and long-term incentive awards, deferred over a three to seven year period in accordance with regulatory requirements. Under the RBS bonus deferral structure, cash awards are limited to £2,000 per employee.

Annual bonus awards

	Senior management	Other MRTs	Total
Number of beneficiaries	—	510	510
	£m	£m	£m
Variable remuneration (cash)	—	1.2	1.2
Deferred remuneration (bonds)	—	11.3	11.3
Deferred remuneration (shares)	—	86.3	86.3

Long-term incentive awards vest subject to the extent to which performance conditions are met and can result in zero payment.

Long-term incentive awards

	Senior management	Other MRTs	Total
Number of beneficiaries	10	98	108
	£m	£m	£m
Long-term incentive awards	17.2	16.2	33.4

The variable component of total remuneration for MRTs at RBS shall not exceed 100% of the fixed component. Based on the information disclosed above, the average ratio between fixed and variable remuneration for 2016 is approximately 1 to 0.6.

3. Outstanding deferred remuneration through 2016

The table below includes deferred remuneration awarded or paid out in 2016 in respect of prior performance years. Deferred remuneration reduced during the year relates to long-term incentives lapsed when performance conditions are not met, long-term incentives and deferred awards forfeited on leaving and malus adjustments of prior year deferred awards and long-term incentives.

Category of deferred remuneration	Senior management £m	Other MRTs £m
Unvested from prior year	34.2	200.8
Awarded during the financial year	17.5	129.4
Paid out	7.4	113.0
Reduced from prior years	1.9	21.8
Unvested at year end	42.4	195.5

4. Sign-on and severance payments

RBS does not operate 'Sign-on awards'. Guaranteed variable remuneration may be used for new hires in compensation for awards foregone in their previous company. Three such payments totalling £442,695 are included in the tables above. This relates to commitments made on recruitment in respect of three new employees. These awards are still subject to deferral.

No severance payments were made during the financial year in excess of contractual payments, local policies, standards or statutory amounts, other than one payment of £219,500 made in commercial settlement of legal proceedings related to the early termination of a contract of employment.

All staff total remuneration

- The average salary for all employees is £32,620.
- 13,664 employees earn between £50,000 and £100,000.
- 5,545 employees earn between £100,000 and £250,000.
- 1,025 employees earn total remuneration over £250,000.

Total remuneration by band for all employees earning >€1 million	Number of employees 2016	Number of employees 2015
€1.0m - €1.5m	48	53
€1.5m - €2.0m	20	24
€2.0m - €2.5m	10	11
€2.5m - €3.0m	5	7
€3.0m - €3.5m	0	2
€3.5m - €4.0m	0	2
€4.0m - €4.5m	3	0
€4.5m - €5.0m	0	1
€5.0m - €6.0m	1	0
€6.0m - €7.0m	0	1
Total	87	101

Notes:

- (1) Total remuneration in the table above includes fixed pay, pension and benefit funding and variable pay (including actual value of LTI vesting in 2016) after the application of malus.
- (2) Executive directors are not included. The table is based on an exchange rate where applicable of €1.224 to £1 as at 31 December 2016 and amounts disclosed for 2015 have been restated using the same exchange rate so that comparison can be made on a like for like basis.

Employees that earned total remuneration of over €1 million in 2016 represent just 0.1% of our employees. This number reduces to 72 employees if we exclude pension and benefit funding. These employees include those who manage major businesses and functions with responsibility for significant assets, earnings or areas of strategic activity and can be grouped as follows:

- The CEOs responsible for each area and their direct reports.
- Employees managing large businesses within a franchise.
- Income generators responsible for high levels of income including those involved in managing trading activity and supporting clients with more complex financial transactions, including financial restructuring.
- Those responsible for managing our balance sheet and liquidity and funding positions across the business.
- Employees managing the successful disposal of assets in Capital Resolution and reducing RBS's capital requirements.

Compliance report

Statement of compliance

RBS is committed to high standards of corporate governance, business integrity and professionalism in all its activities.

Throughout the year ended 31 December 2016, RBS has complied with all of the provisions of the UK Corporate Governance Code issued by the Financial Reporting Council dated April 2016 (the "Code") except in relation to provision (D.2.2) that the Group Performance and Remuneration Committee should have delegated responsibility for setting remuneration for the Chairman and executive directors. RBS considers that this is a matter which should rightly be reserved for the Board and this is an approach RBS has adopted for a number of years. Remuneration for the executive directors is first considered by the Group Performance and Remuneration Committee which then makes recommendations to the Board for consideration. This approach allows all non-executive directors, and not just those who are members of the Group Performance and Remuneration Committee, to participate in decisions on the executive directors' and the Chairman's remuneration and also allows the executive directors to input to the decision on the Chairman's remuneration. The Board believes this approach is very much in line with the spirit of the Code and no director is involved in decisions regarding his or her own remuneration. We do not anticipate any changes to our approach on this aspect of the Code. Information on how RBS has applied the main principles of the Code can be found in the Corporate governance report on pages 57 to 111. A copy of the Code can be found at www.frc.org.uk

RBS has also implemented the recommendations arising from the Walker Review and complied in all material respects with the Financial Reporting Council Guidance on Audit Committees issued in September 2012 and April 2016.

Under the US Sarbanes-Oxley Act of 2002, specific standards of corporate governance and business and financial disclosures and controls apply to companies with securities registered in the US. RBS complies with all applicable sections of the US Sarbanes-Oxley Act of 2002, subject to a number of exceptions available to foreign private issuers.

Internal control

The Board of Directors is responsible for the system of internal controls that is designed to maintain effective and efficient operations, compliant with applicable laws and regulations. The system of internal controls is designed to manage, or mitigate, risk to an acceptable residual level rather than eliminate it entirely. Systems of internal control can only provide reasonable and not absolute assurance against material misstatement, fraud or loss.

Ongoing processes for the identification, evaluation and management of the principal risks faced by RBS operated throughout the period from 1 January 2016 to 23 February 2017, the date the directors approved the Annual Report & Accounts. These processes include the semi-annual Control Environment Certification process which requires senior members of the executive and management to assess the adequacy and effectiveness of their internal control frameworks and certify that their business or function is compliant with the requirements of Sarbanes-Oxley Section 404 and the UK Corporate Governance Code Section C2. The policies that govern these processes – and reports on internal controls arising from them – are reviewed by the Board and meet the requirements of the Financial Reporting Council's Guidance On Risk Management Internal Control & Related Financial & Business Reporting issued in September 2014.

RBS operates a three lines of defence model, which provides a framework for responsibilities and accountabilities across the organisation. As part of its second line of defence role, the Risk function oversees and challenges the firm-wide management of risk and the efficacy of the related controls. In addition, the Risk function is responsible for developing material risk policies and strategic frameworks for the business to use.

The effectiveness of RBS's internal controls is reviewed regularly by the Board, the Group Audit Committee and the Board Risk Committee. Internal Audit undertakes independent assurance activities and provides reports to the committees of Board and executive management on the quality and effectiveness of governance, risk management and internal controls to monitor, manage and mitigate risks in achieving the bank's objectives. In addition, the Board receives risk management reports at each scheduled Board meeting. Executive management committees in each of the RBS businesses also receive regular reports on significant risks facing their business and how they are being controlled. Details of the bank's approach to risk management are given in the Capital & Risk Management section.

RBS has made progress strengthening the control environment in recent years. However, more work is required and RBS continues on its journey of improvement, building on the established control environment, strengthening and remediating where appropriate. Areas of particular focus during 2016 included further work to develop and enhance the risk appetite framework in support of a robust and holistic control approach. In parallel with this, progress was made in further embedding a consistent end-to-end risk and control assessment process. These activities, together with complementary work-streams aimed at developing, enhancing and embedding a strong and dynamic risk culture across each of the franchises and functions, will continue in 2017.

Compliance report

The remediation of known control issues remained an important focus of the Group Audit Committee and the Board Risk Committee during 2016. For further information on their oversight of remediation of the most significant issues, please refer to the Report of the Group Audit Committee and the Report of the Board Risk Committee. The Group Audit Committee has received confirmation that management has taken, or is taking, action to remedy significant failings or weaknesses identified through RBS's control framework. The Group Audit Committee and the Board Risk Committee will continue to focus on such remediation activity, particularly in view of the transformation agenda.

While not being part of the bank's system of Internal control, the bank's independent auditors present to the Group Audit Committee reports that include details of any significant internal control deficiencies they have identified. Further, the system of internal controls is also subject to regulatory oversight in the UK and overseas. Additional details of regulatory oversight are given in the Capital & Risk Management section.

Internal control over financial reporting

RBS is required to comply with Section 404 of the US Sarbanes-Oxley Act of 2002 and assess the effectiveness of internal control over financial reporting as of 31 December 2016.

RBS has assessed the effectiveness of its internal control over financial reporting as of 31 December 2016 based on the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission in the 2013 publication of 'Internal Control - Integrated Framework'.

Based on its assessment, management has concluded that, as of 31 December 2016, RBS's internal control over financial reporting is effective.

RBS's auditors have audited the effectiveness of RBS's internal control over financial reporting and have given an unqualified opinion.

Management's report on RBS's internal control over financial reporting will be filed with the Securities and Exchange Commission as part of the 2016 Annual Report on Form 20-F.

Disclosure controls and procedures

As required by US regulations, management (including the Chief Executive and Chief Financial Officer) have conducted an evaluation of the effectiveness and design of RBS's disclosure controls and procedures (as defined in the Exchange Act rules) as at 31 December 2016. Based on this evaluation, management (including the Chief Executive and Chief Financial Officer) concluded that RBS's disclosure controls and procedures were effective as of the end of the period covered by this annual report.

Changes in internal control

There was no change in RBS's internal control over financial reporting that occurred during the period covered by this report that has materially affected, or is reasonably likely to materially affect, RBS's internal control over financial reporting.

The New York Stock Exchange

As a foreign private issuer with American Depository Shares representing ordinary shares, preference shares and debt securities listed on the New York Stock Exchange (the "NYSE"), RBS is not required to comply with all of the NYSE standards applicable to US domestic companies (the "NYSE Standards") provided that it follows home country practice in lieu of the NYSE Standards and discloses any significant ways in which its corporate governance practices differ from the NYSE Standards. RBS is also required to provide an Annual Written Affirmation to the NYSE of its compliance with the mandatory applicable NYSE Standards.

The Group Audit Committee fully complies with the mandatory provisions of the NYSE Standards (including by reference to the rules of the Exchange Act) that relate to the composition, responsibilities and operation of audit committees. In March 2016 RBS submitted its required annual written affirmation to the NYSE confirming its full compliance with those and other applicable provisions. More detailed information about the Group Audit Committee and its work during 2016 is set out in the Group Audit Committee report on pages 71 to 78.

RBS has reviewed its corporate governance arrangements and is satisfied that these are consistent with the NYSE Standards, subject to the following departures: (i) NYSE Standards require the majority of the Board to be independent. The NYSE Standards contain different tests from the Code for determining whether a director is independent. RBS follows the Code's requirements in determining the independence of its directors and currently has 9 independent non-executive directors, one of whom is the senior independent director (ii) The NYSE Standards require non-management directors to hold regular sessions without management present and that independent directors meet at least once a year. The Code requires the Chairman to hold meetings with non-executive directors without the executives present and non-executive directors are to meet without the Chairman present at least once a year to appraise the Chairman's performance and RBS complies with the requirements of the Code. (iii) The NYSE Standards require that the nominating/corporate governance committee of a listed company be composed entirely of independent directors.

Compliance report

The Chairman of the Board is also the Chairman of the Group Nominations and Governance Committee, which is permitted under the Code (since the Chairman was considered independent on appointment). The terms of reference of the Group Nominations and Governance Committee differ in certain limited respects from the requirements set out in the NYSE Standards, including because the Group Nominations and Governance Committee does not have responsibility for overseeing the evaluation of management (iv) The NYSE standards require that the compensation committee of a listed company be composed of entirely of independent directors. Although the members of the Group Performance and Remuneration Committee are deemed independent in compliance with the provisions of the Code, the Board has not assessed the independence of the members of the Group Performance and Remuneration Committee and the Group Performance and Remuneration Committee has not assessed the independence of any compensation consultant, legal counsel or other adviser, in each case, in accordance with the independence tests prescribed by the NYSE Standards.

The NYSE Standards require that the compensation committee must have direct responsibility to review and approve the Chief Executive's remuneration. As stated at the start of this Compliance Report, in the case of RBS, the Board, rather than the Group Performance and Remuneration Committee, reserves the authority to make the final determination of the remuneration of the Chief Executive (v) The NYSE Standards require listed companies to adopt and disclose corporate governance guidelines. Throughout the year ended 31 December 2016, RBS has complied with all of the provisions of the Code (subject to the exception described above) and the Code does not require RBS to disclose the full range of corporate governance guidelines with which it complies (vi) The NYSE Standards require listed companies to adopt and disclose a code of business conduct and ethics for directors, officers and employees, and promptly disclose any waivers of the code for directors or executive officers. RBS has adopted a code of conduct which applies to all directors, officers and employees and is supplemented by a number of key policies and guidance dealing with matters including , among others, anti-bribery and corruption, anti-money laundering, sanctions, confidentiality, inside information, health, safety and environment, conflicts of interest, market conduct and management records. The Code of Conduct is available to view on RBS's website at rbs.com.

This Compliance report forms part of the Corporate governance report and the Report of the directors.

Report of the directors

The directors present their report together with the audited accounts for the year ended 31 December 2016.

Group structure

The company is a holding company owning the entire issued ordinary share capital of The Royal Bank of Scotland plc, the principal direct operating subsidiary undertaking of the company. Details of the principal subsidiary undertakings of the company are shown in Note 7 on pages 396 and 397. A full list of subsidiary undertakings of the company is shown in Note 15 on pages 400 to 415.

Following placing and open offers in December 2008 and in April 2009, HM Treasury (HMT) owned approximately 70.3% of the enlarged ordinary share capital of the company. In December 2009, the company issued a further £25.5 billion of new capital to HMT in the form of B shares. HMT sold 630 million of its holding of the company's ordinary shares in August 2015. In October 2015 HMT converted its entire holding of 51 billion B shares into 5.1 billion new ordinary shares of £1 each in the company.

The final dividend payment on the Dividend Access Share (DAS) owned by HMT of £1.2 billion was paid in March 2016, effecting the immediate retirement of the DAS which was redesignated as a single B share and subsequently cancelled.

At 31 December 2016, HMT's holding in the company's ordinary shares was 71.3%.

RBS Group ring-fencing

The UK ring-fencing legislation requiring the separation of essential banking services from investment banking services will take effect from 1 January 2019.

To comply with these requirements it is RBS's intention to place the majority of the UK and Western European banking business in ring-fenced banking entities under an intermediate holding company. NatWest Markets will be a separate non ring-fenced bank and The Royal Bank of Scotland International (Holdings) Limited (RBSI Holdings) will also be placed outside the ring-fence, both as direct subsidiaries of RBSG.

The final ring-fenced legal structure and the actions to be taken to achieve it, remain subject to, amongst other factors, additional regulatory, Board and other approvals as well as employee information and consultation procedures. All such actions and their respective timings may be subject to change, or additional actions may be required, including as a result of external and internal factors including further regulatory, corporate or other developments.

On 1 January 2017 RBS made a number of key changes to the legal entity structure as detailed below to support the move towards a ring-fenced structure. There are also plans to make further changes prior to 1 January 2019.

NatWest Holdings Limited (NatWest Holdings)

RBS introduced an intermediate holding company, NatWest Holdings, as a direct subsidiary of RBS plc. This is an interim structure as NatWest Holdings is expected to become a direct subsidiary of RBSG in mid 2018.

National Westminster Bank Plc (NatWest) and Adam & Company Group PLC (Adam & Co) transferred from being direct subsidiaries of RBS plc, and Ulster Bank (Ireland) Holdings Unlimited Company (UBIH) transferred from being a direct subsidiary of Ulster Bank Limited, to become direct subsidiaries of NatWest Holdings.

RBS International

RBSI Holdings transferred from being an indirect subsidiary of RBS plc to become a direct subsidiary of RBSG. The intention is for RBS International's operating companies to remain as subsidiaries of RBSI Holdings.

NatWest bought Lombard North Central PLC and RBS Invoice Finance (Holdings) Limited from RBS plc and some smaller companies from other members of the Group.

Business structure

RBS continues to deliver on its plan to build a strong, simple and fair bank for both customers and shareholders. On 5 December 2016 the Corporate & Institutional Banking (CIB) business was re-branded as NatWest Markets (NWM) in readiness for our future ring-fenced structure; this included the renaming of the reportable operating segment as NatWest Markets. NatWest Markets will continue to offer financing, rates and currencies products to its customers. During 2016 RBS's activities were organised on a franchise basis as follows:

Personal & Business Banking (PBB) comprises two reportable segments, UK Personal & Business Banking (UK PBB) and Ulster Bank RoI. UK PBB serves individuals and mass affluent customers in the UK together with small businesses (generally up to £2 million turnover). UK PBB includes Ulster Bank customers in Northern Ireland. Ulster Bank RoI serves individuals and businesses in the Republic of Ireland (RoI).

Commercial & Private Banking (CPB) comprises three reportable segments, Commercial Banking, Private Banking and RBS International (RBSI). Commercial Banking serves commercial and corporate customers in the UK and Western Europe. Private Banking serves UK connected high net worth individuals and RBSI serves retail, commercial, corporate and financial institution customers in Jersey, Guernsey, Isle of Man and Gibraltar and financial institution customers in Luxembourg.

Report of the directors

NatWest Markets, formerly Corporate and Institutional Banking (CIB), serves UK and Western Europe corporate customers, and global financial institutions, supported by trading and distribution platforms in the UK, US and Singapore.

Capital Resolution was established to execute the sale or wind down of most of the global footprint, from 38 countries to 13, and trade finance and cash management outside the UK and Ireland. Additionally non-strategic markets, portfolio and banking assets identified are being sold or wound down.

Williams & Glyn (W&G) refers to the business formerly intended to be divested as a separate legal entity and comprises RBS England and Wales branch-based businesses, along with certain small and medium enterprises and corporate activities across the UK. During the periods presented W&G has not operated as a separate legal entity. The perimeter of the segment currently reported does not include certain portfolios that were intended to be divested such as the Scottish branch based activity of NatWest and NatWest Business Direct.

Central items & other includes corporate functions, such as RBS treasury, finance, risk management, compliance, legal, communications and human resources. Central functions manages RBS capital resources and RBS-wide regulatory projects and provides services to the reportable segments. Balances in relation to Citizens and the international private banking business are included in Central items in the relevant periods.

Results and dividends

The loss attributable to the ordinary shareholders of the Group for the year ended 31 December 2016 amounted to £6,955 million compared with a loss of £1,979 million for the year ended 31 December 2015, as set out in the consolidated income statement on page 290.

The company did not pay a dividend on ordinary shares in 2014, 2015 or 2016.

In the context of prior macro-prudential policy discussions, the Board decided to partially neutralise any impact on Core Tier 1 capital of coupon and dividend payments in respect of 2015 and 2016 Group hybrid capital instruments through equity issuances of c.£300 million. Consequently, approximately £300 million was raised during 2015 and 2016 through the issue of new ordinary shares and the Board has decided a further £300 million of new equity will be issued during the course of 2017 to again partially neutralise the CET1 impact of coupon and dividend payments.

The Dividend Access Share (DAS) retirement agreement was approved at the General Meeting of shareholders held on 25 June 2014. The first dividend payment on the DAS of £320 million was made in the third quarter of 2014. The balance of £1.2 billion was paid to HMT in March 2016, effecting the immediate retirement of the DAS which was redesignated as a single B share and subsequently cancelled, further normalising the capital structure of RBS and removing an obstacle toward the resumption of capital distributions.

Business review

Activities

RBS is engaged principally in providing a wide range of banking and other financial services. Further details of the organisational structure and business overview of RBS, including the products and services provided by each of its operating segments and the competitive markets in which they operate are contained in the Business review on pages 124 to 162. Details of the strategy for delivering the company's objectives can be found in the Strategic report.

Risk factors

RBS's future performance and results could be materially different from expected results depending on the outcome of certain potential risks and uncertainties. Full details of these and other risk factors are set out on pages 431 to 463.

The reported results of RBS are also sensitive to the accounting policies, assumptions and estimates that underlie the preparation of its financial statements. Details of RBS's critical accounting policies and key sources of accounting judgments are included in Accounting policies on pages 297 to 308.

RBS's approach to risk management, including its financial risk management objectives and policies and information on RBS's exposure to price, credit, liquidity and cash flow risk, is discussed in the Capital and risk management section.

Financial performance

A review of RBS's performance during the year ended 31 December 2016, including details of each operating segment, and RBS's financial position as at that date is contained in the Business review on pages 124 to 162.

RBS Holdings N.V. (formerly ABN AMRO Holding N.V.)

In 2007, RFS Holdings B.V., which was jointly owned by RBS, the Dutch State (successor to Fortis) and Santander completed the acquisition of ABN AMRO Holding N.V.

Report of the directors

Following the announcements in April 2011 by the Boards of RBSG, RBS plc, RBS Holdings and RBS N.V., a substantial part of the business activities of RBS N.V. had been successfully transferred to RBS plc by 2014. There is continued focus on further de-risking the RBS N.V. balance sheet. Ultimately, the objective is that RBS N.V. is in a position to relinquish its banking licence in the Netherlands.

Business divestments

To comply with the European Commission State Aid requirements RBS agreed a series of restructuring measures. These include the sale of 80.01% of RBS's Global Merchant Services business (completed in 2010), the sale of substantially all of the RBS Sempra Commodities joint venture business (largely completed in 2010), the divestment of Direct Line Insurance Group plc (completed in 2014), as well as the divestment of the RBS branch-based business in England and Wales and the NatWest branches in Scotland, along with the direct SME customers across the UK ("UK branch-based businesses").

During 2016 work has continued to explore means to achieve separation and divestment of the business previously described as Williams & Glyn. On 17 February 2017, RBS announced that it had been informed by HM Treasury (HMT) that the Commissioner responsible for EU competition policy plans to propose to the College of Commissioners to open proceedings to gather evidence on an alternative plan for RBS to meet its remaining State Aid obligations. If adopted, this alternative plan would replace the existing requirement to achieve separation and divestment by 31 December 2017 of the business previously described as Williams & Glyn.

As previously disclosed, none of the proposals to acquire the business received by RBS can deliver full separation and divestment before the 31 December 2017 deadline. As RBS no longer intends to pursue divestment of Williams & Glyn by way of an Initial Public Offering, the £600 million exchangeable bond issued to a consortium of investors, led by Centerbridge and Corsair, was redeemed on 21 October 2016 in accordance with the terms of the bond.

RBS completed its divestment of Citizens Financial Group Inc (IPO completed in 2015).

Employees

Our colleagues

As at 31 December 2016, RBS employed 77,900 people (full-time equivalent basis, including temporary workers) throughout the world. Details of related costs are included in Note 3 on the consolidated accounts.

Building a healthy culture

Building a healthy culture that embodies Our Values is one of our core priorities.

Our Values guide the way we identify the right people to serve our customers well, and how we manage, engage and reward our colleagues. They are at the heart of both Our Standards (the bank wide behavioural framework) and Our Code (the bank wide Code of Conduct).

To really live our values we continue to reinforce them in our systems, our policies and processes, our communications, training and leadership role modelling.

We monitor our progress against our goals. We gather feedback from our colleagues, and through metrics and key performance indicators to assess our progress and respond accordingly. We do this in tandem with feedback from regulators and industry bodies.

Engaging our colleagues

We know that building an engaged, healthy and inclusive workforce is crucial to achieving our ambition. Every year we ask our colleagues to share their thoughts on what it's like to work here via our annual colleague survey (OurView). The results help us monitor levels of engagement and enable our people leaders to work with their teams to make improvements. It also helps us measure the progress we are making towards our goals.

Our most recent survey, in which almost 63,000 colleagues took part, showed that we are changing the culture of RBS for the better. We remain above the global financial services norm for wellbeing, our inclusion scores continue to improve and there is a strong sense that managers act consistently with Our Values. However, the choices we've had to make as we move RBS forward have taken a toll on our colleagues. The scaling down of RBS and the impact of dealing with some difficult legacy issues have contributed to a decline in the improvements in engagement, pride and leadership that we saw in 2015.

Rewarding our colleagues

Our approach to performance management provides clarity for our colleagues about how their contribution links to our ambition. It recognises behaviour that supports our values and holds individuals to account for behaviour and performance that does not. In 2016 we refreshed our behavioural framework to create one framework for all our colleagues.

We have a focus on paying the right wage to colleagues and our rates of pay continue to exceed the Living Wage Foundation Benchmarks.

At the start of 2016 we removed sales incentives and we gave every eligible frontline colleague in Personal & Business Banking an increase to their guaranteed pay. This approach remains popular with our colleagues and ensures that our customers can be certain that if they take a product from us, it has no financial impact on what our colleagues are paid.

For 2017, we have simplified how we pay our clerical colleagues, consolidating bonuses, making pay fairer and easier to understand.

Report of the directors

We remain focused on our goals in relation to gender equality and have played an active role in the consultation process for upcoming Gender Pay Gap Reporting regulations. We intend to comply fully with the regulations and to make a public disclosure during 2017.

Developing our colleagues

In 2015, we launched 'Determined to Lead', a core management system for RBS. It is the means by which leaders put our values into practice every day and is transforming the way we operate by creating a common language, consistent operating rhythm and improving the competence of our leaders across RBS. It provides consistent tools to lead and engage our colleagues. This programme has continued in 2016 with over 16,000 leaders participating in the programme.

In October 2016 we launched Service Excellence training, our new customer service programme. The first module introduces our Core Service Behaviours and provides an awareness of the tools and techniques that will help us to deliver the best possible service, every time. Service Excellence gives us a shared service language and the behaviours to help us achieve our ambition. Since October over 34,000 colleagues have completed this module.

Professionalising our colleagues is important to us. We work closely with the Chartered Banker Institute (CBI) and Chartered Banker Professional Standards Board (CB:PSB) to offer our colleagues professional qualifications. Over 8,000 of our colleagues completed their CBI qualification in 2016.

We are especially pleased that we achieved an Excel rating in the CB:PSB Foundation Standard review for 2015. We are one of only two CB:PSB member firms to have secured 'Earned Autonomy' - meaning we are exempt from quarterly monitoring over the next 3 years. 95% of our in-scope population have achieved the Foundation Standard. This is a great reflection of the focus we continue to place on professionalising our colleagues.

We also offer a wide range of learning which can be mandatory, role specific or related to personal development. Our mandatory learning has to be completed by everyone and is focused on keeping our our customers, colleagues and RBS safe.

Youth employment

In 2016 we welcomed over 500 people across our Graduate and Apprenticeship schemes, 40% being female hires.

Health and wellbeing of our colleagues

Wellbeing is a big part of how we create a great place to work.

We offer a wide range of health benefits and services to help maintain physical and mental health, and support our colleagues if they become unwell.

In 2016, we focused on physical, mental health and social wellbeing. We participated in the Global Corporate Challenge (GCC) - more than 50,000 colleagues took part helping us to win the GCC World Most Active Organisation Gold Award. We also continued to promote Lifeworks (RBS's Employee Assistance Programme) and launched our Mindfulness toolkit. We continued our support of Time to Change (the UK's biggest programme to challenge mental health stigma).

Employee consultation

We recognise employee representatives such as trade unions and work councils in a number of businesses and countries. There has been ongoing engagement and discussion with those bodies given the scale of change taking place across RBS. Management have continued to meet regularly with our European Employee Council to discuss developments and update on the progress of our strategic plans.

Inclusion

Building a more inclusive RBS is essential for our customers and colleagues. Our inclusion policy standard applies to all our colleagues globally.

During 2016, we continued to roll out unconscious bias learning to all our colleagues to create a solid platform for the wider inclusion agenda. Almost 30,000 colleagues participated in unconscious bias training in 2016 meaning we have trained around 66,000 colleagues across RBS to date.

We continue to work towards our goal of having at least 30% senior women in our top three leadership layers across each Franchise and Function by 2020 and to be fully gender balanced (50/50) by 2030. We have a positive action approach in place, tailored by business, according to the specific challenges they face.

Our disability plan will support us becoming a disability smart organisation by 2018. It addresses areas for improvement including branch access, accessible services, improving colleague adjustment processes and inserting disability checkpoints into our key processes and practices.

We continue to focus on building an ethnically diverse RBS. Our plan focuses on positive action and includes reciprocal mentoring, targeted development workshops and leadership programmes and ensuring we have a Black, Asian and Minority Ethnic (BAME) focus on recruitment, talent identification and promotion.

Our LGBT agenda continues to deliver a better experience for our LGBT colleagues and customers. We have processes in place to support updating gender and title on customers' banking records and to support colleagues undergoing gender transition. And, we continue to support our 16,000 strong employee-led networks.

Report of the directors

We have been recognised for our work on Equality, Diversity and Inclusion by our Platinum ranking from Opportunity Now (gender), our Gold ranking for Race for Opportunity (race); retaining a position in the Times Top 50 Employers for Women; becoming a Top Ten Global Employer in Stonewall's Global Equality Index (LGBT), Silver Status from The Business Disability Forum and being rated a Top 10 Employer by Working Families.

Sustainability

Our purpose is to serve customers well. We will rebuild our reputation and earn our customers' trust by putting customers first, making RBS a great place to work, supporting our communities and being mindful of environmental impacts. The Sustainable Banking Committee's role is to support the Board in overseeing, supporting and challenging actions being taken by management to run RBS as a sustainable business.

For more information on our approach and progress please read the RBS Strategic Report. Further information is available on rbs.com/sustainability.

Greenhouse gas emissions

Disclosures relating to greenhouse gas emissions are included in the Strategic Report on page 35.

Going concern

RBS's business activities and financial position, the factors likely to affect its future development and performance and its objectives and policies in managing the financial risks to which it is exposed and its capital are discussed in the Business review. The risk factors which could materially affect RBS's future results are set out on pages 432 to 463. RBS's regulatory capital resources and significant developments in 2016 and anticipated future developments are detailed on pages 178 to 186. The liquidity and funding section on pages 187 to 198 describes RBS's funding and liquidity profile, including changes in key metrics and the build up of liquidity reserves.

Having reviewed RBS's forecasts, projections and other relevant evidence, the directors have a reasonable expectation that RBS and the company will continue in operational existence for the foreseeable future. Accordingly, the financial statements of RBS and of the company have been prepared on a going concern basis.

Viability statement

Under the revised UK Corporate Governance Code the directors are required to confirm that they have carried out a robust assessment of the RBS's principal risks and make a longer term viability statement. This is set out in the Strategic Report on page 55.

BBA disclosure code

RBS's 2016 financial statements have been prepared in compliance with the principles set out in the Code for Financial Reporting Disclosure published by the British Bankers' Association in 2010. The Code sets out five disclosure principles together with supporting guidance. The principles are that RBS and other major UK banks will provide high quality, meaningful and decision-useful disclosures; review and enhance their financial instrument disclosures for key areas of interest to market participants; assess the applicability and relevance of good practice recommendations to their disclosures acknowledging the importance of such guidance; seek to enhance the comparability of financial statement disclosures across the UK banking sector; and clearly differentiate in their annual reports between information that is audited and information that is unaudited.

Enhanced Disclosure Task Force (EDTF)

The EDTF established by the Financial Stability Board, published its report 'Enhancing the Risk Disclosures of Banks' in October 2012. All EDTF recommendations are reflected in the 2016 Annual Report and Accounts and Pillar 3 Report.

Corporate governance

The company is committed to high standards of corporate governance. Details are given in the Corporate governance report on pages 57 to 111. The Corporate governance report and compliance report (pages 112 to 114) form part of this Report of the directors.

Share capital

Details of the ordinary and preference share capital at 31 December 2016 and movements during the year are shown in Note 25 on the consolidated accounts.

During 2016, the company allotted and issued a total of 142.2 million new ordinary shares of £1 each for the purposes of ensuring 2016 coupon payments on discretionary hybrid capital securities were partly neutralised from a Core Tier 1 capital perspective. The shares were allotted to UBS AG at the subscription prices determined by reference to the average market prices during the sale periods set out below.

Number of shares sold	Subscription price	Sale period	Gross proceeds	Share price on allotment
37.6m	226.250p	26/2/16-14/4/16	£85 million	231.6p
38.5m	220.687p	29/4/16-24/5/16	£85 million	245.3p
35.5m	196.924p	05/8/16-02/09/16 28/10/16-	£70 million	204.3p
30.6m	195.930p	16/11/16	£60 million	208.4p

In the three years to 31 December 2016, the percentage increase in issued share capital due to non-pre-emptive issuance (excluding employee share schemes) for cash was 2.71%.

In addition, the company issued 56 million shares in connection with employee share schemes during 2016.

Report of the directors

In October 2015, HMT converted its entire holding of 51 billion B shares into 5.1 billion new ordinary shares of £1 each

In March 2016, the company paid a final dividend of £1.2 billion in respect of the Dividend Access Share (DAS) held by HMT, effecting the immediate retirement of the DAS which was redesignated as a single B share and subsequently cancelled.

Authority to repurchase shares

At the Annual General Meeting in 2016 shareholders authorised the company to make market purchases of up to 1,166,108,903 ordinary shares. The directors have not exercised this authority to date. Shareholders will be asked to renew this authorisation at the Annual General Meeting in 2017.

Additional information

Where not provided elsewhere in the Report of the directors, the following additional information is required to be disclosed by Part 6 of Schedule 7 to the Large and Medium-sized Companies and Groups (Accounts and Reports) Regulations 2008.

The rights and obligations attached to the company's ordinary shares and preference shares are set out in the company's Articles of Association, copies of which can be obtained from Companies House in the UK or can be found at rbs.com/about/board-and-governance.

On a show of hands at a general meeting of the company every holder of ordinary shares and cumulative preference shares present in person or by proxy and entitled to vote shall have one vote. On a poll, every holder of ordinary shares or cumulative preference shares present in person or by proxy and entitled to vote shall have four votes for every share held. The notices of Annual General Meetings and General Meetings specify the deadlines for exercising voting rights and appointing a proxy or proxies to vote in relation to resolutions to be passed at the meeting.

The cumulative preference shares represent less than 0.008% of the total voting rights of the company, the remainder being represented by the ordinary shares.

There are no restrictions on the transfer of ordinary shares in the company other than certain restrictions which may from time to time be imposed by laws and regulations (for example, insider trading laws).

Pursuant to the Listing Rules of the FCA, certain employees of the company require the approval of the company to deal in the company's shares.

The rules governing the powers of directors, including in relation to issuing or buying back shares and their appointment are set out in the company's Articles of Association. It will be proposed at the 2017 Annual General Meeting that the directors be granted authorities to allot shares under the Companies Act 2006. The company's Articles of Association may only be amended by a special resolution at a general meeting of shareholders.

The rights and obligations of holders of non-cumulative preference shares are set out in Note 25 on the consolidated accounts.

The company is not aware of any agreements between shareholders that may result in restrictions on the transfer of securities and/or voting rights. There are no persons holding securities carrying special rights with regard to control of the company.

A number of the company's employee share plans include restrictions on transfers of shares while shares are subject to the plans or the terms under which the shares were awarded.

Under the rules of certain employee share plans, eligible employees are entitled to acquire shares in the company, and shares are held in trust for participants by The Royal Bank of Scotland plc and Ulster Bank Dublin Trust Company as Trustees. Voting rights are exercised by the Trustees on receipt of participants' instructions. If a participant does not submit an instruction to the Trustee no vote is registered.

The Royal Bank of Scotland plc 1992 Employee Share Trust, The Royal Bank of Scotland Group plc 2001 Employee Share Trust and The Royal Bank of Scotland Group plc 2007 US Employee Share Trust hold shares on behalf of RBS's employee share plans. The voting rights are exercisable by the Trustees, however, in accordance with investor protection guidelines, the Trustees abstain from voting. The Trustees would take independent advice before accepting any offer in respect of their shareholdings for the company in a takeover bid situation.

Awards granted under the company's employee share plans may be met through a combination of newly issued shares and shares acquired in the market by the company's employee benefit trusts.

A change of control of the company following a takeover bid may cause a number of agreements to which the company is party to take effect, alter or terminate. All of the company's employee share plans contain provisions relating to a change of control. Outstanding awards and options may vest and become exercisable on change of control, subject where appropriate to the satisfaction of any performance conditions at that time and pro-rating of awards. In the context of the company as a whole, these agreements are not considered to be significant.

Directors

The names and brief biographical details of the current directors are shown on pages 58 to 61.

Sandy Crombie, Howard Davies, Alison Davis, Morten Friis, Robert Gillespie, Penny Hughes, Ross McEwan, Brendan Nelson, Baroness Noakes and Ewen Stevenson all served throughout the year and to the date of signing of the financial statements.

Report of the directors

Mike Rogers was appointed to the Board on 26 January 2016 and Frank Dangeard was appointed on 16 May 2016.

All directors of the company are required to stand for election or re-election annually by shareholders at the Annual General Meeting and, in accordance with the UK Listing Rules, the election or re-election of independent directors requires approval by all shareholders and also by independent shareholders.

Directors' interests

The interests of the directors in the shares of the company at 31 December 2016 are shown on page 105. None of the directors held an interest in the loan capital of the company or in the shares or loan capital of any of the subsidiary undertakings of the company, during the period from 1 January 2016 to 23 February 2017.

Directors' indemnities

In terms of section 236 of the Companies Act 2006 (the "Companies Act"), Qualifying Third Party Indemnity Provisions have been issued by the company to its directors, members of the RBS Executive Committee, individuals authorised by the PRA/FCA and certain directors and/or officers of RBS subsidiaries.

In terms of section 236 of the Companies Act, Qualifying Pension Scheme Indemnity Provisions have been issued to all trustees of RBS pension schemes.

Post balance sheet events

Other than the matter disclosed on page 390, there have been no significant events between the year end and the date of approval of these accounts which would require a change to or disclosure in the accounts.

Controlling shareholder

In accordance with the UK Listing Rules, the company has entered into an agreement with HM Treasury (the 'Controlling Shareholder') which is intended to ensure that the Controlling Shareholder complies with the independence provisions set out in the UK Listing Rules. The company has complied with the independence provisions in the relationship agreement and as far as the company is aware the independence and procurement provisions in the relationship agreement have been complied with in the period by the controlling shareholder.

Shareholdings

The table below shows shareholders that have notified RBS that they hold more than 3% of the total voting rights of the company at 31 December 2016.

Solicitor For The Affairs of Her Majesty's Treasury as Nominee for Her Majesty's Treasury	Number of shares (millions)	% of share class held	% of total voting rights held
Ordinary shares	8,434	71.3	71.3

As at 23 February 2017, there were no changes to the shareholdings shown in the table above.

Listing Rule 9.8.4

In accordance with the UK Financial Conduct Authority's Listing Rules the information to be included in the Annual Report and Accounts under LR 9.8.4, is set out in this Directors' report with the exception of details of contracts of significance under LR 9.8.4. (10) and (11) given in Additional Information on pages 430 to 431.

Political donations

At the Annual General Meeting in 2016, shareholders gave authority under Part 14 of the Companies Act, for a period of one year, for the company (and its subsidiaries) to make political donations and incur political expenditure up to a maximum aggregate sum of £100,000. This authorisation was taken as a precaution only, as the company has a longstanding policy of not making political donations or incurring political expenditure within the ordinary meaning of those words. During 2016, RBS made no political donations, nor incurred any political expenditure in the UK or EU and it is not proposed that RBS's longstanding policy of not making contributions to any political party be changed. Shareholders will be asked to renew this authorisation at the Annual General Meeting in 2017.

Directors' disclosure to auditors

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

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

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

Auditors

EY LLP are the auditors. EY were appointed to fill the casual vacancy arising from Deloitte LLP's resignation following the signing of the 2015 accounts and the Group's Form 20-F and appointed by shareholders at the 2016 Annual General Meeting. A resolution to reappoint EY as the company's auditors will be proposed at the forthcoming Annual General Meeting.

By order of the Board

Aileen Taylor
Company Secretary
23 February 2017

The Royal Bank of Scotland Group plc
is registered in Scotland No. SC45551

Statement of directors' responsibilities

This statement should be read in conjunction with the responsibilities of the auditor set out in their report on pages 278 to 289.

The directors are responsible for the preparation of the Annual Report and Accounts. The directors are required by Article 4 of the IAS Regulation (European Commission Regulation No 1606/2002) to prepare Group accounts, and as permitted by the Companies Act 2006 have elected to prepare company accounts, for each financial year in accordance with International Financial Reporting Standards as adopted by the European Union. They are responsible for preparing accounts that present fairly the financial position, financial performance and cash flows of the Group and the company. In preparing those accounts, the directors are required to:

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

The directors are responsible for keeping proper accounting records which disclose with reasonable accuracy at any time the financial position of the Group and to enable them to ensure that the Annual Report and Accounts complies with the Companies Act 2006. They are also responsible for safeguarding the assets of the Group and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

The directors confirm that to the best of their knowledge:

- the financial statements, prepared in accordance with International Financial Reporting Standards, give a true and fair view of the assets, liabilities, financial position and profit or loss of the company and the undertakings included in the consolidation taken as a whole; and
- the Strategic Report and Directors' report (incorporating the Business review) include a fair review of the development and performance of the business and the position of the company and the undertakings included in the consolidation taken as a whole, together with a description of the principal risks and uncertainties that they face.

In addition, the directors are of the opinion that the Annual Report and Accounts, taken as a whole, is fair, balanced and understandable and provides the information necessary for shareholders to assess the company's position and performance, business model and strategy.

By order of the Board

Howard Davies
Chairman

Ross McEwan
Chief Executive

Ewen Stevenson
Chief Financial Officer

23 February 2017

Board of directors

Chairman

Howard Davies

Executive directors

Ross McEwan
Ewen Stevenson

Non-executive directors

Sandy Crombie
Frank Dangeard
Alison Davis
Morten Friis
Robert Gillespie
Penny Hughes
Brendan Nelson
Baroness Noakes
Mike Rogers