RBS Citizens
Financial Group, Inc.™

Investor Report

RBS Citizens Financial Group, Inc.

December 31, 2013

To the holders of the 4.15% Subordinated Notes due 2022

Issued under, and pursuant to the terms of, an indenture dated as of September 28, 2012 between RBS Citizens Financial Group, Inc. and The Bank of New York Mellon, as Trustee

RBS Citizens Financial Group, Inc. is a subsidiary of The Royal Bank of Scotland Group plc. This report is being provided to the holders of the 4.15% Subordinated Notes due 2022 (the "Subordinated Notes") issued by RBS Citizens Financial Group, Inc. under the terms of the Subordinated Note Indenture dated as of September 28, 2012 between RBS Citizens Financial Group, Inc., as issuer, and The Bank of New York Mellon, as Trustee, as amended, supplemented or modified from time to time. This report is not intended for any other purpose.

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GLOSSARY OF ACRONYMS AND TERMS

The following listing provides a comprehensive reference of common acronyms and terms used throughout the document:

AFS	Available For Sale
ALLL	Allowance For Loan and Lease Losses
AOCI	Accumulated Other Comprehensive Income
ATM	Automatic Teller Machine
BHC	Bank Holding Company
bps	Basis Points
Capital Plan Rule	Federal Reserve's Regulation Y Capital Plan Rule
CCB	Capital Conservation Buffer
CCAR	Comprehensive Capital Analysis and Review
CEB	Commercial Enterprise Banking
CET1	Common Equity Tier 1
CLTV	Combined Loan-to-Value
CMO	Collateralized Mortgage Obligation
CRA	Community Reinvestment Act of 1977
CSA	Credit Support Annex
Dodd-Frank Act (DFA)	The Dodd-Frank Wall Street Reform and Consumer Protection Act of 2010
EC	Economic Capital
ERISA	Employee Retirement Income Security Act of 1974
Fannie Mae (FNMA)	The Federal National Mortgage Association
FASB	The Financial Accounting Standards Board
FDIC	Federal Deposit Insurance Corporation
FDICIA	Federal Deposit Insurance Corporation Improvement Act of 1991
FHC	Financial Holding Company
FHLB	Federal Home Loan Bank
FICO	Fair Isaac Corporation (credit rating)
FLSA	Fair Labor Standards Act of 1938, as amended
FRB	Federal Reserve Bank
FRBG	Federal Reserve Board of Governors
Freddie Mac (FHLMC)	The Federal Home Loan Mortgage Corporation
GDP	Gross Domestic Product
Ginnie Mae (GNMA)	The Government National Mortgage Association
GLBA	Gramm-Leach-Bliley Act of 1999
HELOC	Home Equity Line of Credit
HTM	Held To Maturity
ICAR	Internal Capital Adequacy Requirement
IFRS	International Financial Reporting Standards
ILP	Incurred Loss Period
IST	Integrated Stress Testing
IT	Information Technology
LIBOR	London Interbank Offered Rate
LOCOM	Lower of Cost or Market
LOB	Line of Business

GLOSSARY OF ACRONYMS AND TERMS

LTV	Loan-to-Value
MBS	Mortgage-Backed Security
MD&A	Management's Discussion and Analysis of Financial Condition and Results of Operation
MERS	Mortgage Electronic Registration Systems, Inc.
MSR	Mortgage Servicing Right
NPR	Notice of Proposed Rulemaking
OCC	Office of the Comptroller of the Currency
OCI	Other Comprehensive Income
OIS	Overnight Index Swap
OTC	Over the Counter
PIMCO	Pacific Investment Management Company, LLC
RBS	The Royal Bank of Scotland plc.
RBS CBFM	The Royal Bank of Scotland plc. Corporate Banking and Financial Markets
RBS Citizens or RBSCFG or the Company	RBS Citizens Financial Group, Inc. and its Subsidiaries
RBSG or RBS Group	The Royal Bank of Scotland Group plc.
REIT	Real Estate Investment Trust
ROTCE	Return on Tangible Common Equity
RPA	Risk Participation Agreement
RV	Recreational Vehicle
SBO	Serviced by Others
SIFI	Systematically Important Financial Institutions
TDR	Troubled Debt Restructuring
UK	United Kingdom
U. S. GAAP	Accounting Principles Generally Accepted in the United States of America

RBS CITIZENS FINANCIAL GROUP, INC.

SELECTED FINANCIAL INFORMATION

SELECTED FINANCIAL DATA

The following tables present selected consolidated historical financial information of RBS Citizens. You should read this information together with the Consolidated Financial Statements, related notes, and the other information included elsewhere in this document. The data for the years ended December 31, 2013, 2012, and 2011, and at December 31, 2013 and 2012 have been derived from the RBS Citizens' audited Consolidated Financial Statements.

	Years ended December 31,		
(dollars in millions)	2013	2012	2011
OPERATING DATA:			
Net interest income	$3,058	$3,227	$3,320
Provision for credit losses	479	413	882
Noninterest income	1,632	1,667	1,711
Noninterest expense	7,679	3,457	3,371
Noninterest expense, excluding goodwill impairment[1]	3,244	3,457	3,371
Income (loss) before income tax expense (benefit)	(3,468)	1,024	778
Income tax expense (benefit)	(42)	381	272
Net income (loss)	(3,426)	643	506
Net income, excluding goodwill impairment[1]	654	643	506
OTHER DATA:			
Return on average tangible assets	(3.05)%	0.55%	0.43%
Return on average tangible assets, excluding goodwill impairment[1]	0.58	0.55	0.43
Return on average tangible common equity	(25.91)	4.86	4.18
Return on average tangible common equity, excluding goodwill impairment[1]	4.95	4.86	4.18
Net interest margin	2.85	2.89	2.97

[1] 2013 noninterest expense, net income (loss), return on average tangible assets, and return on average tangible common equity were calculated excluding the $4.4 billion pretax ($4.1 billion after tax) goodwill impairment recorded in June, and accordingly, these are non-GAAP financial measures.

(dollars in millions)	December 31, 2013	December 31, 2012
BALANCE SHEET DATA:		
Total assets	$122,154	$127,053
Securities	21,245	19,417
Total loans and leases	85,859	87,248
Allowance for loan and lease losses	1,221	1,255
Goodwill	6,876	11,311
Deposits	86,903	95,148
Federal funds purchased and securities sold under agreements to repurchase	4,791	3,601
Borrowed funds	3,656	1,195
Stockholder's equity	19,196	24,129
OTHER DATA:		
Capital ratios		
Tier 1	13.5%	14.2%
Total	16.1	15.8
Leverage ratio	11.6	12.1

MANAGEMENT'S DISCUSSION & ANALYSIS OF FINANCIAL CONDITION & RESULTS OF OPERATIONS

The following MD&A provides information that management believes will assist in understanding the financial performance of RBS Citizens. You should read the MD&A together with the Consolidated Financial Statements and the Notes to Consolidated Financial Statements.

FORWARD-LOOKING STATEMENTS

The information included in this report contains certain forward-looking statements. These forward-looking statements may relate to the Company's financial condition, results of operations, plans, objectives, future performance and business, including, but not limited to, statements with respect to expected earnings levels, the adequacy of the allowance for credit losses, delinquency trends, market risk and the impact of interest rate changes, capital market conditions, capital adequacy and liquidity, the effect of legal proceedings, and new accounting standards on the Company's financial condition and results of operations. All statements contained herein that are not clearly historical in nature are forward-looking, and the words "anticipate," "believe," "continues," "expect," "estimate," "intend," "project" and similar expressions and future or conditional verbs such as "will," "would," "should," "could," "might," "can," "may," or similar expressions are generally intended to identify forward-looking statements.

Forward-looking statements are not guarantees of future performance, are based on management's current expectations and, by their nature, involve certain risks, uncertainties, estimates and assumptions by management that are difficult to predict. Various factors, some of which are beyond the Company's control, could cause actual results to differ materially from those expressed in, or implied by, such forward-looking statements. Factors that might cause such a difference include, but are not limited to:

- the rate of growth in the economy and employment levels, as well as general business and economic conditions;
- changes in interest rates and market liquidity, as well as the magnitude of such changes, which may reduce interest margins, impact funding sources and affect the ability to originate and distribute financial products in the primary and secondary markets;
- changes in federal bank regulatory and supervisory policies, including required levels of capital;
- the impact of the DFA on the Company's businesses, business practices and costs of operations;
- the relative strength or weakness of the retail and commercial credit sectors and of the real estate markets in the markets in which the Company's borrowers are located;
- competition in the financial services industry; and
- legislative, tax, accounting or regulatory changes.

Other possible events or factors that could cause results or performance to differ materially from those expressed in such forward-looking statements include the following:

- negative economic conditions that adversely affect the general economy, housing prices, the job market, consumer confidence and spending habits which may affect, among other things, the level of nonperforming assets, charge-offs and provision expense;
- adverse movements and volatility in debt and equity capital markets;
- changes in market rates and prices, which may adversely impact the value of financial assets and liabilities;
- liabilities resulting from litigation and regulatory investigations;
- the Company's ability to grow its core businesses;

- decisions to downsize, sell or close units or otherwise change the Company's business mix; and
- management's ability to identify and manage these and other risks.

All forward-looking statements included in this document are based upon information available to the Company as of the date of this document, and other than as required by law, including the requirements of applicable securities laws. The Company assumes no obligation to update or revise any such forward-looking statements to reflect occurrences or unanticipated events or circumstances after the date of such statements.

INTRODUCTION

RBS Citizens is a BHC and FHC headquartered in Providence, Rhode Island, and through its subsidiaries has more than 1,400 branches, approximately 3,500 ATMs, and nearly 19,000 employees. Its two bank subsidiaries, RBS Citizens, N.A. and Citizens Bank of Pennsylvania, operate a twelve-state branch network under the Citizens Bank brand in Connecticut, Delaware, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Vermont, and under the Charter One brand in Illinois, Michigan and Ohio.

RBS Citizens is a wholly-owned subsidiary of The Royal Bank of Scotland plc, a banking subsidiary of the ultimate parent, The Royal Bank of Scotland Group plc. On December 1, 2008, the UK Government became the ultimate controlling party of RBS Group. The UK Government's shareholding is managed by UK Financial Investments Limited, a company wholly owned by the UK Government. RBS Group reports the results of RBS Citizens' core businesses as "U.S. Retail and Commercial" and non-core assets as "Non-Core" in its published financial statements in accordance with IFRS, as defined by the International Accounting Standards Board.

The financial position and results of operations included herein are prepared in accordance with U.S. GAAP and represent all of RBS Citizens' assets, including its non-core assets. RBS Citizens' non-core assets include those loans and other assets that management considers to be outside of the Company's core business strategy. See the "Non-Core Assets" section below for further detail.

EXECUTIVE OVERVIEW

RBS Citizens reported net income of $152 million for the quarter, up 50% from $101 million in the fourth quarter of 2012. For the year ended December 31, 2013, RBS Citizens recorded a $4.4 billion pre-tax goodwill impairment charge that resulted in a $3.4 billion net loss. Net income, excluding the impact of the goodwill impairment charge recorded in the second quarter, was $654 million, up $11 million or 2% from 2012. Return ratios have stabilized and are beginning to grow, with ROTCE at 4.71% in the fourth quarter, up from 2.94% in the fourth quarter of 2012. The full year ROTCE was 4.95%, excluding the impact of the goodwill impairment charge, up from 4.86% last year.

Fourth Quarter Highlights

- In January 2014, the Company announced that it had reached an agreement to sell 94 Charter One branches in the Chicago area, including $5.3 billion of local deposits and $1.1 billion in locally originated loans.
- RBS Group announced the intention to accelerate its plans for a partial initial public offering of RBS Citizens in the second half of 2014, and to fully divest the Company by the end of 2016.

Discussion of Results:

Income Statement (dollars in millions)	**4Q 2013**	**3Q 2013**	**4Q 2012**
Net interest income	$779	$770	$772
Provision for credit losses	132	145	103
Noninterest income	379	383	390
Noninterest expense	818	788	895
Net income	152	144	101
Net interest margin	2.83%	2.88%	2.80%

Favorable overall performance was achieved, indicated by net income of $152 million for the quarter, up 50% from $101 million in the fourth quarter of 2012. Full year net income, excluding the impact of the goodwill impairment charge recorded in the second quarter, was $654 million, up $11 million or 2% from 2012.

Net interest income was $779 million in the fourth quarter, up from $772 million in the fourth quarter of 2012, with margin at 2.83%, up 3 basis points, driven by lower interest expense for deposits (down 45%) and fed funds and repos (down 18%). Full year net interest income was $3.1 billion, down 5% from 2012 and is proportional to the smaller average balance sheet. Full year margin was 2.85%, reflecting the continued challenges in the low rate environment. Recent increases in commercial loan average balances and yield are helping margin results.

Noninterest income was $379 million in the fourth quarter, down 3% from the fourth quarter of 2012. Increases in other income, net gains on sales of securities, and trust and investment services revenue were more than offset by declining mortgage banking fees and service charges on deposits. The Company is holding more of its loan originations for portfolio rather than selling them, which is reflected in the mortgage banking results. Full year noninterest income was $1.6 billion, down 2% from 2012 driven by the same reasons as the quarter movements.

Noninterest expense was $818 million for the fourth quarter, down 9% from the fourth quarter of 2012. A one-time pension charge of $77 million in 2012 was the primary reason for the decline. Higher occupancy expense was offset by lower equipment expense and lower other operating expense. Full year noninterest expense was $7.7 billion, compared to $3.5 billion in 2012, driven by a current year goodwill impairment charge of $4.4 billion. Excluding the one-time charges for pension and goodwill, expenses are lower, driven by lower other operating expenses partially offset by higher software amortization, occupancy and outside services.

Balance Sheet (dollars in billions)	**4Q 2013**	**3Q 2013**	**4Q 2012**
Average investment securities	$22.9	$21.0	$22.5
Average loans	85.8	84.5	86.6
Average deposits	93.2	93.1	94.3

Loans

Average loans increased $1.3 billion, or 2% compared to prior quarter primarily due to a $1.0 billion increase in commercial loans and a $0.5 billion increase in residential mortgages, offset by a $0.2 billion decrease in the home equity serviced by others portfolio.

Average loans decreased $0.8 billion, or 1%, compared to the fourth quarter of last year. The decline was primarily driven by a $1.5 billion decrease in the home equity loan portfolio and $0.9 billion in home equity lines of credit portfolio. These declines were offset by a $1.6 billion increase in commercial loans.

In January 2014, RBS Citizens announced that it had reached an agreement to sell 94 Charter One branches in the Chicago area, including $1.1 billion in locally originated loans which are reported in loans held for sale at year end. The announced sale had an immaterial impact on average loans. This sale is expected to close in the second quarter of 2014.

Investment securities

As of December 31, 2013, the Company's securities portfolio totaled $21.2 billion. The securities available for sale portfolio, which is the largest component of the portfolio, was $16.0 billion, a decrease of $3.9 billion from September 30, 2013, and a decrease of $2.4 billion from December 31, 2012. During the fourth quarter of 2013, the Company transferred $4.2 billion of available for sale securities to held to maturity.

Deposits

Average deposits for the fourth quarter of 2013 experienced a slight decrease in the higher cost deposit products category but overall remained consistent with the prior quarter at $93.1 billion. In keeping with the company's strategy to reduce higher cost deposits, money market and term deposits continued to decline while demand deposits increased.

When compared to the fourth quarter of last year, the average deposits in the fourth quarter of 2013 decreased $1.1 billion, or 1%, primarily a result of the Company's strategic decision to runoff its higher cost deposit products in the term and money market product categories. Average demand deposits increased $545 million, or 2%, while interest-bearing deposit accounts decreased $1.7 billion, or 2%, primarily due to a decline in term deposits and money market accounts.

The Company recently announced that it had reached an agreement to sell 94 Charter One branches in the Chicago area, including $5.3 billion in deposits which are reported in deposits held for sale at year end. The announced sale had an immaterial impact on average deposits. This sale is expected to close in the second quarter of 2014.

Capital

Capital ratios continue to be well above current regulatory requirements, with Total Capital at 16.1%, up from 15.8% a year ago, and Tier 1 Capital at 13.5%. The Company continues to have historically high asset liquidity levels provided in the form of a large core deposit base and other available funding resources, as well as cash.

During the fourth quarter, the Company issued $334 million of 10-year 4.691% fixed-rate, fixed maturity subordinated notes to RBSG, and also paid a $334 million special dividend and a $40 million regular dividend to RBS.

RESULTS OF OPERATIONS

NET INCOME (LOSS)

RBS Citizens reported net income of $152 million for the quarter, up 50% from $101 million in the fourth quarter of 2012. The Company reported a net loss of $3.4 billion for the year ended December 31, 2013, after recording a goodwill impairment charge of $4.4 billion in the second quarter. Excluding this non-cash charge, the Company would have recognized net income of $654 million, up from $643 million in 2012. During 2012, the Company accrued $138 million to settle litigation related to overdraft fee practices, charged $77 million to noninterest expense following a lump sum payment made to vested former employees of the defined benefit plan, and realized a one-time gain of $75 million on the sale of Visa shares.

NET INTEREST INCOME

The following tables show the major components of net interest income and net interest margin:

	Years Ended												
	December 31, 2013			December 31, 2012			December 31, 2011			Increase (Decrease) From 2013-2012		Increase (Decrease) From 2012-2011	
(dollars in millions)	Average Balances	Income/ Expense	Yields/ Rates	Average Balances	Income/ Expense	Yields/ Rates	Average Balances	Income/ Expense	Yields/ Rates	Average Balances	Yields/ Rates	Average Balances	Yields/ Rates
Assets													
Investments	$21,352	$488	2.29%	$23,632	$624	2.64%	$24,763	$757	3.06%	($2,280)	(0.35)%	($1,131)	(0.42)%
Commercial	28,654	900	3.10	27,273	849	3.07	23,886	779	3.22	1,381	0.03	3,387	(0.15)
Commercial real estate	6,568	178	2.67	7,063	196	2.72	8,310	237	2.82	(495)	(0.05)	(1,247)	(0.10)
Leases	3,463	105	3.05	3,216	112	3.48	2,952	113	3.83	247	(0.43)	264	(0.35)
Total commercial loans	38,685	1,183	3.02	37,552	1,157	3.04	35,148	1,129	3.18	1,133	(0.02)	2,404	(0.14)
Home equity lines of credit	17,105	485	2.83	17,745	497	2.80	17,172	472	2.75	(640)	0.03	573	0.05
Residential mortgage	9,104	360	3.96	9,551	413	4.32	9,721	453	4.66	(447)	(0.36)	(170)	(0.34)
Home equity loans	6,330	361	5.71	8,176	481	5.88	10,575	627	5.93	(1,846)	(0.17)	(2,399)	(0.05)
Automobile	8,857	235	2.65	8,276	273	3.30	7,541	339	4.50	581	(0.65)	735	(1.20)
Student and other installment loans	3,655	202	5.52	4,040	218	5.38	4,863	259	5.32	(385)	0.14	(823)	0.06
Credit cards	1,669	175	10.46	1,634	166	10.15	1,580	155	9.79	35	0.31	54	0.36
Total retail loans	46,720	1,818	3.89	49,422	2,048	4.14	51,452	2,305	4.48	(2,702)	(0.25)	(2,030)	(0.34)
Total loans and leases	85,405	3,001	3.50	86,974	3,205	3.67	86,600	3,434	3.95	(1,569)	(0.17)	374	(0.28)
Loans held for sale	392	12	3.07	538	17	3.10	359	13	3.70	(146)	(0.03)	179	(0.60)
Total earning assets	107,149	3,501	3.25	111,144	3,846	3.45	111,722	4,204	3.75	(3,995)	(0.20)	(578)	(0.30)
Allowance for loan and lease losses	(1,219)			(1,506)			(1,888)			287		382	
Goodwill and other intangibles	9,437			11,323			11,344			(1,886)		(21)	
Other non earning assets	5,499			6,705			7,166			(1,206)		(461)	
Total non earning assets	13,717			16,522			16,622			(2,805)		(100)	
Total assets	$120,866			$127,666			$128,344			($6,800)		($678)	
Liabilities and Stockholder's Equity													
Checking with interest	$14,096	$8	0.06%	$13,522	$10	0.08%	$16,116	$15	0.10%	$574	(0.02)%	($2,594)	(0.02)%
Money market & savings	42,575	105	0.25	41,249	121	0.29	37,638	94	0.25	1,326	(0.04)	3,611	0.04
Term deposits	11,266	103	0.91	13,534	244	1.80	16,501	381	2.31	(2,268)	(0.89)	(2,967)	(0.51)
Total interest-bearing deposits	67,937	216	0.32	68,305	375	0.55	70,255	490	0.70	(368)	(0.23)	(1,950)	(0.15)
Federal funds purchased and securities sold under agreements to repurchase [1]	2,400	192	7.89	2,716	119	4.31	3,808	191	4.96	(316)	3.58	(1,092)	(0.65)
Short-term borrowed funds	251	4	1.64	3,026	101	3.27	2,459	150	6.04	(2,775)	(1.63)	567	(2.77)
Long-term borrowed funds	778	31	3.93	1,976	24	1.20	5,085	53	1.02	(1,198)	2.73	(3,109)	0.18
Total borrowed funds	3,429	227	6.53	7,718	244	3.11	11,352	394	3.42	(4,289)	3.42	(3,634)	(0.31)
Total interest-bearing liabilities	71,366	443	0.61	76,023	619	0.80	81,607	884	1.07	(4,657)	(0.19)	(5,584)	(0.27)
Total demand deposits	25,399			25,053			21,191			346		3,862	
Other liabilities	2,267			2,652			2,409			(385)		243	
Stockholder's equity	21,834			23,938			23,137			(2,104)		801	
Total liabilities and stockholder's equity	$120,866			$127,666			$128,344			($6,800)		($678)	
Interest rate spread			2.64%			2.65%			2.68%				
Net interest income		$3,058			$3,227			$3,320		($169)		($93)	
Net interest margin			2.85%			2.89%			2.97%		(0.04)%		(0.08)%

[1] Balances are net of certain short-term receivables associated with reverse repurchase agreements; interest expense includes the full cost of the repurchase agreements and certain hedging costs.

For the year ended December 31, 2013, net interest income was $3.1 billion and net interest margin was 2.85%. This reflects a decline of $169 million and 4 bps when compared to the year ended December 31, 2012. The decline was driven by a continuation of historically low interest rates, which led to a decline in earning asset yields greater than the ability to reduce interest-bearing liabilities costs. On the assets side, net average loan balances decreased $1.6 billion in 2013 compared to 2012 and interest on loans decreased $204 million during the same period. Yields on earning assets declined 20 bps compared to the same period last year, as yields on the investment portfolio and loan portfolio declined 35 bps and 17 bps, respectively from 2012. Declines are attributed to run-off and prepayment of higher-yielding, fixed rate assets and new purchases/originations with lower yields.

At December 31, 2013, the Company currently has $1.5 billion in higher cost, legacy pay-fixed interest-rate swaps tied to Federal Funds. Hedge accounting for these swaps and the underlying hedged items affect both RBS Citizens' deposit costs and borrowing costs. The hedge documentation allows for hedging of various types of borrowed funds and certain deposit balances. These swaps originally hedged deposits and borrowed funds, with the cost of the hedges allocated between these two categories. Over time, the deposit balances that were hedged have diminished, leaving the cost of the remaining swaps to be borne by the remaining borrowed funds balances. In addition, when permitted by U.S. GAAP, the Company nets short-term receivables associated with its reverse repurchase agreements with short-term payables associated with its repurchase agreements, while associated income is not netted. As a result, the net yield including securities sold for repurchase agreement and hedge costs appears high at 7.89%.

The overall pay-fixed swap expense noted above declined to $201 million for the year ended December 31, 2013 compared to $290 million in 2012. Over the same time, the notional swap balances have matured by $2.2 billion to a remaining balance of $1.5 billion.

Total interest-bearing deposit costs, excluding the hedge costs, were 0.30% and 0.43% for the years ended December 31, 2013 and 2012, respectively. Many deposit products have hit pricing floors at or near zero, limiting further rate reductions and thus compressing margin. Excluding the impact of the hedging expense assigned to term deposits, the rates were 0.80% and 1.20% for the years ended December 31, 2013 and 2012, respectively. Excluding the impact of the hedge expense and the netting of repurchase agreement balances, total borrowed funds rates were 3.11% and 3.47% for the years ended December 31, 2013 and 2012, respectively. The increase in borrowing costs can be attributed to new subordinated debt issuances in 2013 of $1 billion yielding 4.69% to 5.16%.

For the year ended December 31, 2012, net interest income was $3.2 billion and net interest margin was 2.89%. This reflects a decline of $93 million and 8 bps when compared to the year ended December 31, 2011. On the assets side, while net average loan balances for the year ended December 31, 2012 increased $374 million compared to the same period in 2011, interest income on loans decreased $229 million. Yields on loans declined 28 bps compared to the same period in the prior year. Additionally, yields on the investment portfolio dropped 42 bps from 2011. Declines are attributed to run-off and prepayment of higher yielding, fixed rate assets and new originations of loans with lower yields as well as sales of higher yielding investment securities. In addition, an increase in prepayments speeds increased net premium amortization expense on investment securities.

On the funding side, interest-bearing deposit expense was reduced by $115 million and deposit costs declined 15 bps. Many deposit products have hit pricing floors at or near zero, limiting further rate reductions and thus compressing margin. However, RBS Citizens' cost of other borrowed funds improved $150 million, or 31 bps, due to maturing legacy fixed rate swaps that carried high pay-fixed interest rates.

PROVISION FOR CREDIT LOSSES

Credit trends continue to improve as net charge-offs decreased by $16 million to $115 million quarter-over-quarter and declined by $75 million from the same quarter last year. On a year-over-year basis, net charge-offs decreased significantly, down $374 million or 43% to $501 million.

The total provision has decreased by $13 million to $132 million quarter-over-quarter, but increasing by $29 million compared to the same quarter last year. On a year-over-year basis, the total provision rose by $66 million, or 16% to $479 million. The rise in the provision for loan losses reflects portfolio growth in the commercial segment and recognition of exposure related to expected HELOC payment shock discussed in further detail in the Retail Asset Quality section of this MD&A.

The total provision for credit losses includes the provision for loan losses as well as the provision for unfunded commitments. The provision for loan losses is the result of a detailed analysis performed to estimate an appropriate and adequate ALLL. Refer to Allowance for Credit Losses and Nonperforming Assets below for more details.

NONINTEREST INCOME

The following table details the significant components of total noninterest income:

	Years Ended December 31,			Increase (Decrease)	Increase (Decrease)
(dollars in millions)	2013	2012	2011	2013-2012	2012-2011
Service charges on deposits	$505	$558	$597	(9)%	(7)%
ATM and debit card	160	169	267	(5)	(37)
Mortgage banking	153	189	62	(19)	205
Trust and investment services revenue	149	131	131	14	—
Net gains on sales of securities available for sale	144	95	162	52	(41)
Other service fee income	135	146	145	(8)	1
International fees	97	105	114	(8)	(8)
Credit card fees	74	80	77	(8)	4
Capital markets fee income	53	52	40	2	30
Bank-owned life insurance	50	51	49	(2)	4
Other income[1]	112	91	67	23	36
Total noninterest income	$1,632	$1,667	$1,711	(2)%	(3)%

[1] Includes net impairment losses on AFS securities recognized in earnings, other net gains, and other income.

Total noninterest income was $1.6 billion for the year ended December 31, 2013, down from the prior year, primarily driven by lower mortgage banking, deposit, ATM and debit card fees offset by net gains on the sales of higher yielding investment securities. Mortgage banking fees decreased $36 million for the year ended December 31, 2013, driven by a decline in sales activity as more loans were kept in portfolio, offset by a higher mortgage servicing rights valuation. ATM and debit card fees decreased $9 million, or 5% for the year ended December 31, 2013 primarily due to lower transaction volumes. Other income for 2012 includes a $75 million gain on the sale of Visa, Inc. Class B shares.

NONINTEREST EXPENSE

The following table displays the significant components of total noninterest expense:

	Years Ended December 31,			Increase (Decrease)[1]	Increase (Decrease)[1]
(dollars in millions)	2013	2012	2011	2013-2012	2012-2011
Salaries and employee benefits	$1,652	$1,743	$1,623	(5)%	7%
Outside services	360	339	340	6	0
Occupancy	327	310	372	5	(17)
Equipment expense	275	279	301	(1)	(7)
Amortization of software	102	77	53	32	45
Deposit insurance	85	98	117	(13)	(16)
Promotional expense	76	86	102	(12)	(16)
Operating losses	60	196	32	(69)	NM
Goodwill impairment	4,435	—	—	NM	NM
Other operating expense	307	329	432	(7)	(24)
Total noninterest expense	$7,679	$3,457	$3,372	122 %	3%
Total noninterest expense excluding goodwill impairment[2]	$3,244	$3,457	$3,372	(6)%	3%

[1] NM - not meaningful

[2] Excludes the $4.4 billion goodwill impairment and is a non-GAAP financial measure.

Total noninterest expense increased $4.2 billion in the year ended December 31, 2013, compared to the year ended December 31, 2012, due to the goodwill impairment described below of $4.4 billion recorded in the second quarter of 2013. Excluding the impact of the impairment, noninterest expense decreased $213 million, or 6% in the year ended December 31, 2013, compared to the year ended December 31, 2012, which included both a $138 million charge to settle overdraft fee litigation that occurred in the first quarter of 2012 and a $77 million lump sum payment made to vested former employees of the defined benefit plan in the fourth quarter of 2012. Excluding the impact of the impairment, litigation, and lump sum payment, noninterest expense remained relatively flat.

U.S. GAAP requires the Company to review goodwill for impairment annually, or more frequently if events or circumstances indicate any of its business units' fair value might be less than its carrying value. RBS Citizens allocates its goodwill to two reporting units - Retail Banking and Commercial Banking.

The valuation of goodwill is dependent on forward-looking expectations related to the performance of the U.S. economy and the associated financial performance of the Company. The prolonged delay in the full recovery of the U.S. economy, and the impact of that delay on earnings expectations, prompted a goodwill impairment test as of June 30, 2013. Although the U.S. economy has demonstrated signs of recovery, notably improvements in unemployment and housing, the pace and extent of recovery in these indicators, as well as in overall GDP, have lagged previous expectations. The impact of the slow recovery is most evident in the Company's Retail Banking reporting unit. The latest forecasted economic growth for the U.S., coupled with the continuing impact of the new regulatory framework in the financial industry, have resulted in a deceleration of expected growth for the Retail Banking reporting unit's future profits, and an associated goodwill impairment.

After recording the impairment charge in the Retail Banking reporting unit, the remaining carrying value of goodwill is $6.9 billion. In 2008, RBS Citizens recorded a similar goodwill impairment charge of $1.5 billion in its U.S. GAAP-based reports and at that time also recorded a $6.4 billion goodwill impairment charge under IFRS in RBS Group's consolidated results. No similar charge is warranted under IFRS in 2013, and the carrying value of RBS Citizens' goodwill under an IFRS basis is now comparable to that reported under U.S. GAAP.

PROVISION FOR INCOME TAXES

The (benefit) provision for income taxes was $(42) million and $381 million, for the years ended December 31, 2013 and 2012, respectively. The provision represents an actual 1% and 37% effective tax rate for the same periods, respectively.

The decrease in the effective rate from 2012 to 2013 represents the tax rate impact of the 2013 goodwill impairment in addition to the tax rate impact of a 2012 state tax settlement. Goodwill not deductible for tax purposes comprised 78.4% of the total goodwill impairment charge and generated a 35% reduction in the effective tax rate for the year ended December 31, 2013. The Company settled a state tax issue for the years 2003 through 2008 related to its real estate investment trust and various passive investment companies.

ANALYSIS OF FINANCIAL CONDITION

SECURITIES

RBS Citizens' securities portfolio is managed to promote the maximization of return while maintaining prudent levels of quality, market risk and liquidity. The following table presents RBS Citizens' AFS and HTM portfolios. See further discussion of the Company's AFS and HTM portfolios in the Consolidated Financial Statements.

	December 31, 2013		December 31, 2012		Increase (Decrease) in Fair Value[1]
(dollars in millions)	Amort. Cost	Fair Value	Amort. Cost	Fair Value	
Available For Sale Securities					
U.S. Treasury	$15	$15	$15	$15	0 %
State and political subdivisions	11	10	20	21	(52)
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	14,970	14,993	16,368	16,904	(11)
Other / non-agency	992	952	1,452	1,397	(32)
Total mortgage-backed securities	15,962	15,945	17,820	18,301	(13)
Total debt securities	15,988	15,970	17,855	18,337	(13)
Marketable equity securities	10	13	5	7	86
Other equity securities	12	12	12	12	—
Total equity securities	22	25	17	19	32
Total available for sale securities	$16,010	$15,995	$17,872	$18,356	(13)%
Held To Maturity Securities					
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	$2,940	$2,907	$0	$0	NM
Other / non-agency	1,375	1,350	—	—	NM
Total held to maturity securities	$4,315	$4,257	$0	$0	NM
Total available for sale and held to maturity securities	$20,325	$20,252	$17,872	$18,356	10 %

[1] NM - not meaningful

During 2013, to reduce the growing potential negative impact of AFS securities market volatility on tangible common equity, the Company transferred a total of $4.2 billion, consisting of federal agency and other non-agency from the AFS portfolio to establish an HTM securities portfolio. At the time of transfer, $134 million of unrealized net losses were recognized in OCI. The amounts in OCI will be recognized in interest income over the remaining life of the securities as an offset to the adjustment of yield in a manner consistent with the amortization of premium and the accretion of discount.

The fair value of the securities portfolio (AFS and HTM) increased by $1.9 billion in the year ended December 31, 2013, or 10%, compared to December 31, 2012. U.S. Government-guaranteed notes and government sponsored entity issued MBS comprise the majority of AFS holdings. Reinvestments have been directed predominantly into fixed rate products; and as of December 31, 2013, the portfolio had an average expected life of 4.6 years. As long-term interest rates rose during the quarter, reinvestment of agency MBS cash flows was higher than in recent prior quarters. The non-agency MBS sector has recently re-opened and reinvestment has once again been directed into this asset class. The recent increase in longer-term rates and improved credit support has prompted the bank to invest in this sector in the third quarter of 2013.

For the twelve months ended December 31, 2013, securities portfolio income (AFS and HTM) was $446 million, down $140 million from 2012, and the yield on the portfolio was 2.50%. The portfolio yield decreased by 38 bps driven by faster prepayments in the MBS portfolio coupled with securities sales programs during the year. MBS cash flows and sales during 2013 totaled $8.2 billion. MBS purchases and reinvestment of cash flows during 2013 totaled $10.7 billion.

LOANS AND LEASES

The following table shows the composition of total loans and leases. See further discussion of the Company's loan and lease portfolio in the Consolidated Financial Statements.

(dollars in millions)	December 31, 2013	December 31, 2012	Increase (Decrease)
Commercial	$28,667	$28,856	(1)%
Commercial real estate	6,948	6,459	8
Leases	3,780	3,415	11
Total commercial	39,395	38,730	2
Residential	29,694	31,101	(5)
Home equity products serviced by others	2,171	2,960	(27)
Other secured retail	10,700	10,568	1
Unsecured retail	3,899	3,889	—
Total retail	46,464	48,518	(4)
Total loans and leases	$85,859	$87,248	(2)%

Excluded from the table above are loans totaling $1.1 billion, which were reclassified to loans held for sale at December 31, 2013. See Note 17 "Divestitures and Branch Assets and Liabilities Held for Sale" for further discussion.

RBS Citizens' loans and leases are disclosed in portfolio segments and classes. The Company's loan and lease portfolio segments are commercial and retail. The classes of loans and leases are: commercial, commercial real estate, leases, residential (includes residential mortgages and home equity loans and lines of credit), home equity products serviced by others (includes certain purchased home equity loans and lines of credit), other secured retail (includes automobile loans and other installment loans), and unsecured retail (includes student loans and credit card).

Loan balances as of December 31, 2013, compared to December 31, 2012, reflect growth in total commercial offset by decreases in total retail, primarily in home equity products serviced by others and residential mortgages.

The following table is a summary of loans and leases by remaining maturity or re-pricing date:

(dollars in millions)	December 31, 2013	December 31, 2012	Increase (Decrease)
Due in one year or less	$46,586	$46,110	1 %
Due after one year through five years	15,953	16,588	(4)
Due after five years	23,320	24,550	(5)
Total loans and leases	$85,859	$87,248	(2)%

ALLOWANCE FOR CREDIT LOSSES & NONPERFORMING ASSETS

Overall Asset Quality

RBS Citizens' portfolio of retail and commercial loans and leases totaled $85.9 billion at year-end 2013, down 2% from $87.2 billion at year-end 2012. The portfolio is discussed in segments consisting of commercial and retail. Reflecting the Company's business strategy to have a more balanced retail and commercial business mix, the commercial portfolio totaled $39.4 billion (or 46% of the total portfolio) at December 31, 2013, up from $38.7 billion, or 44%, of the total portfolio at year-end December 31, 2012. The retail portfolio declined to $46.5 billion (54% of the total portfolio) over the same period.

To address retail portfolio attrition, several growth initiatives were undertaken during 2013 that were primarily aimed at keeping credit quality stable by looking for deeper relationships with existing quality customers and examining additional opportunities within current credit guidelines.

The allowance for credit losses at December 31, 2013 remained flat at $1.3 billion year-over-year. Overall credit performance is measured in terms of the net charge-off rate (net loans charged off as uncollectible as a percentage of total average loans and leases), delinquency rate (total loans and leases past due 30 or more days as a percentage of total loans and leases), nonperforming loans & leases ratio (nonperforming loans & leases as a percentage of total loans & leases), and criticized commercial loans (consisting of special mention, substandard and doubtful) as a percentage of total loans and leases. For commercial loans and leases, the Company utilizes regulatory classification ratings to monitor credit quality. Loans with a "pass" rating are those that the Company believes will be fully repaid in accordance with the contractual loan terms. Commercial loans and leases that are "criticized" are those that have some weakness that indicates an increased probability of future loss. For retail loans, the Company primarily uses the loan's payment and delinquency status to monitor credit quality. The further a loan is past due, the greater the likelihood of future credit loss. These credit quality indicators for both commercial and retail loans are continually updated and monitored.

The total loan portfolio credit performance continued to improve across all credit measures in 2013. The portfolio net charge-off rate fell to 0.59% in 2013, and is much improved from 1.01% in 2012. The delinquency rate improved to 1.9% in December 2013 from 2.5% at year-end 2012. Nonperforming loans fell to 1.7% ($1.4 billion) of the portfolio in December 2013 versus 2.1% ($1.9 billion) in December 2012. Approximately $607 million ($77 million in commercial and $530 million of retail) of nonperforming loans attract no specific reserve at December 31, 2013, as these are largely TDRs that have already been charged down to market value. Removing the TDRs (with zero reserve) from the nonperforming loans increased the allowance to nonperforming loans ratio to 151% at December 31, 2013 from 106% at December 31, 2012.

The sustained credit improvement in the commercial portfolio benefited from consistent underwriting and from the recovering economy, along with the continued efforts to manage down loans that were no longer core to the bank's business strategy. In the retail portfolio, consistently high quality originations offset the deterioration in the balloon home equity product, which saw a rise in delinquency. Management took steps to address this industry wide phenomenon as discussed in the retail asset section below.

Commercial Asset Quality

RBS Citizens' commercial portfolio consists of traditional commercial and commercial real estate businesses. The portfolio is focused primarily on high quality, in-footprint customers where the Company's local delivery model provides for strong client connectivity with its bank subsidiaries.

Modest growth of $665 million, or 2%, was achieved in the commercial portfolio from December 31, 2012 with the portfolio ending at $39.4 billion at December 31, 2013. Meanwhile, non-core assets continued to decrease, down 41% to $489 million for the year ended December 31, 2013.

During 2013, the quality of the portfolio improved. Total criticized loans were down 37.0% from year-end 2012 to 4.9% of the commercial portfolio versus 7.9% in 2012. Commercial real estate classified balances declined 59.8% and now represent 3.5% of the commercial real estate portfolio balance, compared to 9.4% at December 31, 2012. Commercial real estate now accounts for 25.6% of the classified loans versus 36.9% a year ago.

Nonperforming balances and charge-offs have displayed a similar positive trend in 2013. Nonperforming commercial balances have declined by $345 million, or 57%, and ended at $265 million with a 60% decline in commercial real estate nonperforming loans. Total commercial nonperforming loans now stand at 0.7% of total commercial loans versus 1.6% at year-end 2012. Likewise, commercial net charge-offs for the year ended December 31, 2013 were $21 million, which was an 85.4% decline from 2012, primarily due to lower gross charge-offs, which were down 58.0%.

Retail Asset Quality

RBS Citizens' retail portfolio remains predominately focused on lending across the New England, Mid-Atlantic, and Midwest regions, with continued geographic expansion in the vehicle secured business. Originations within the footprint are primarily initiated through the branch network, whereas out-of-footprint lending is driven by dealer networks (indirect auto).

The retail portfolio totaled $46.5 billion as of December 31, 2013; a decrease of $2.1 billion, or 4.2%, from December 31, 2012, driven by continued run-off of the non-core SBO portfolio and general attrition in the home equity portfolio. This decrease was partially offset by continued growth in vehicle secured lending and opportunistic whole loan residential mortgage purchases. These distribution models are centered in relationship, either customer or dealer based, which attract a higher quality applicant pool.

The credit composition of the portfolio remained favorable and well-positioned across all product lines with an average refreshed FICO of 754 (Prime) as of December 31, 2013, unchanged from a year ago. Real estate CLTV of 67.8% as of December 31, 2013 compared favorably with CLTV of 74.8% as of December 31, 2012. Excluding the SBO portfolio, the real estate CLTV was 65.1% as of December 31, 2013 and 71.4% as of December 31, 2012. The favorable reduction in CLTV was driven by recent improvements in home values and higher quality originations.

The full year net charge-off rate (core and non-core) of 1.0% in 2013, decreased 45 bps from the prior year, driven by SBO and RV / Marine. The overall rate of delinquency more than 30 days past due improved 36 bps to 2.6% as of December 31, 2013 from 3.0% as of December 31, 2012. The improvement was driven by portfolio mix and lower delinquencies in segments of residential loans, partially offset by deterioration in HELOC. Elevated delinquency rates in the HELOC portfolio can be attributed to a slowdown in foreclosure cycle time and the effects of payment shock for maturing customers exiting their ten-year interest only draw period. These customers face either a final balloon payment or increased payment associated with contractual amortization. To manage the effects of payment shock, a comprehensive plan was developed to proactively mitigate the $3.1 billion (18% of the total HELOC portfolio) of current balances (conventional and balloon) expected to mature by December 2015 (down from $5.0 billion in the first quarter of 2012). The mitigation plan includes enhanced communications with borrowers through direct mailing, email campaigns and out-bound calling to provide alternative financing options and loan modifications.

Nonperforming loans of 2.5% as of December 31, 2013 improved 11 bps from December 31, 2012. The improvement in nonperforming retail loans was primarily driven by the return of $178 million of current non-accruing residential mortgage TDR loans to accruing status in December 2013. In general, nonaccruing TDRs can be returned to accruing status after a sustained period of performance if the loan is supported by a well documented evaluation of the borrower's financial condition. Refer to the discussion of Nonperforming Loans and Leases in Note 1 of the Consolidated Financial Statements for more information.

NON-CORE ASSETS

Non-core assets are primarily loans that do not fit the current strategy of RBS Citizens due to geographic location, industry or product type. These loans have been actively managed down since June 30, 2009. Since designating certain loans and other assets as non-core in 2009, RBS Citizens has run-off approximately $8.8 billion, charged off $3.8 billion, returned $2.8 billion to the core portfolio, and sold $1.3 billion. Non-core balances have now declined over 81% since the designation of the non-core portfolios. During 2013, total non-core assets have continued to decline with balances of $3.8 billion at year-end, down $1.9 billion, or 33% compared to the prior year-end. Commercial non-core balances are down 41% compared to the prior year end at $489 million while the larger retail balances of $3.3 billion have reduced $1.5 billion, or 32%. The larger than normal decrease was driven by a non-core to core transfer of $677 million of conforming student, SBO and residential mortgage loans. Non-core assets are expected to continue to decline through a combination of the factors described above.

The table below is a composition of RBS Citizens' non-core assets as of the dates indicated:

(dollars in millions)	December 31, 2013	December 31, 2012	(Date of Designation) June 30, 2009	Decrease from 2012	Decrease from 2009
Commercial	$108	$187	$1,900	(42)%	(94)%
Commercial real estate	381	643	3,412	(41)	(89)
Total commercial	489	830	5,312	(41)	(91)
Residential mortgages	705	1,012	2,082	(30)	(66)
Home equity products serviced by others	2,160	2,897	6,180	(25)	(65)
Other secured retail	—	—	4,037	—	(100)
Unsecured retail	406	869	2,490	(53)	(84)
Total retail	3,271	4,778	14,789	(32)	(78)
Other assets	81	106	378	(24)	(79)
Total non-core assets	$3,841	$5,714	$20,479	(33)%	(81)%

SBO Portfolio

The SBO portfolio is a liquidating portfolio consisting of pools of home equity loans and lines of credit purchased between 2003 and 2007. The SBO book has been closed to new purchases since the third quarter of 2007, with exposure down to $2.2 billion as of December 31, 2013 from $2.9 billion as of December 31, 2012. This portfolio represents 7% of the entire retail real estate portfolio and 4.6% of the overall retail portfolio as of December 31, 2013. The SBO portfolio had a full year charge-off rate of 5.4% through December 31, 2013 and a cumulative charge-off rate of 26.4% as of December 31, 2013. The elevated charge-off rate is attributed to out-of-footprint geographies (CA, NV, AZ, and FL), high (95%) second lien concentration, and high loan-to-value exposure. Performance on SBO continues to improve with delinquencies and losses decreasing steadily. The 90+ delinquency rate continues to trend lower at 1.8% as of December 31, 2013, a 14 bps reduction from December 31, 2012. The continued improvement in performance is driven by portfolio liquidation (the weakest loans have been charged off), as well as more effective account servicing and collection strategies.

DEPOSITS

The table below presents RBS Citizens' major components of deposits. See further discussion of the Company's deposits in Note 10 to the Consolidated Financial Statements.

(dollars in millions)	December 31, 2013	December 31, 2012	Increase (Decrease)
Demand	$24,931	$25,931	(4)%
Checking with interest	13,630	14,577	(6)
Regular savings	7,509	7,874	(5)
Money market accounts	31,245	35,102	(11)
Term deposits	9,588	11,664	(18)
Total deposits	$86,903	$95,148	(9)%

Total deposits at December 31, 2013 were $86.9 billion, compared with $95.1 billion at December 31, 2012. The decrease of $8.2 billion, or 9%, was primarily due to $5.3 billion in deposits that were reclassified to deposits held for sale at December 31, 2013. See Note 17 "Divestitures and Branch Assets and Liabilities Held for Sale" for further discussion.

Excluding the impact of the deposits held for sale reclassification, total deposits at December 31, 2013 compared to December 31, 2012 would have been lower by approximately $3.0 billion or 3% over the period. Term deposits decreased $1.2 billion, or 10%, reflecting the continued run-off of higher cost term deposits. Money market accounts decreased 5% from December 31, 2012. All other deposit balances were flat year over year.

BORROWED FUNDS

The tables below present the Company's borrowed funds. See further discussion of RBS Citizens' borrowed funds in the Consolidated Financial Statements.

The following is a summary of the Company's short-term borrowed funds:

	Years Ended December 31,	
(dollars in millions)	2013	2012
Federal funds purchased	$689	$1,905
Securities sold under agreements to repurchase	4,102	1,696
Short-term borrowed funds	2,251	501
Total short-term borrowed funds	$7,042	$4,102

Key data related to short-term borrowed funds is presented in the following table:

	Years Ended December 31,		
(dollars in millions)	2013	2012	2011
Weighted average interest rate at year-end			
Federal funds purchased and securities sold under agreements to repurchase	0.09%	0.10%	0.06%
Short-term borrowed funds	0.20	0.29	0.20
Maximum amount outstanding at month-end during the year			
Federal funds purchased and securities sold under agreements to repurchase	$5,114	$4,393	$6,406
Short-term borrowed funds	2,251	5,050	4,000
Average amount outstanding during the year			
Federal funds purchased and securities sold under agreements to repurchase	$2,400	$2,716	$3,808
Short-term borrowed funds	259	3,045	2,645
Weighted average interest rate during the year			
Federal funds purchased and securities sold under agreements to repurchase	0.31%	0.22%	0.12%
Short-term borrowed funds	3.10	2.46	2.65

The following is a summary of the Company's long-term borrowed funds:

	As of December 31,	
(dollars in millions)	2013	2012
Parent company:		
4.150% subordinated debt, due 2022	$350	$350
5.158% subordinated debt, due 2023	333	—
4.771% subordinated debt, due 2023	333	—
4.691% subordinated debt, due 2024	334	—
1.860% subordinated debt, due 2035	—	289
Subsidiary		
Federal Home Loan advances due through 2033	25	27
Other	30	28
Total long-term debt	$1,405	$694

Short-term unsecured borrowed funds are minimal and are offset by $1.3 billion in average excess reserves held at the FRB at December 31, 2013. Other borrowed funds include capital instruments and secured FHLB advances. Additionally, asset liquidity is considered strong. At December 31, 2013, unencumbered high-quality securities totaled $10.5 billion; unused FHLB capacity was approximately $8.2 billion; and unencumbered loans pledged at the FRBs created additional contingent borrowing capacity of approximately $10.4 billion.

Asset liquidity is at historically high levels and access to funds has been available through repurchase agreements, collateralized borrowed funds, or asset sales. Additionally, there is capacity to grow deposits. While access to short-term wholesale markets is limited, the Company has been able to meet its funding needs for the medium term with deposits and collateralized borrowed funds.

DERIVATIVES

Historically, RBS Citizens has used "plain vanilla" pay-fixed swaps to synthetically lengthen liabilities, offsetting duration in fixed-rate assets. With material prepayment of fixed-rate mortgages and home equity loans since 2008, these swaps were no longer needed. Most have been terminated or allowed to run-off.

The Company implemented a new hedging program during the quarter ended March 31, 2013 to help partially offset the margin gap created by a downsized investment portfolio and reduce overall balance sheet asset sensitivity. The Company uses "plain vanilla" receive-fixed swaps to minimize the exposure to variability in the interest cash flows on its floating rate assets. This is reflected in the interest rate swaps line in the table below. As of December 31, 2013, $4 billion receive-fixed swaps had been executed. The assets and liabilities for derivatives designated as hedges reflect the market value of these hedge instruments.

The Company also sells interest rate swaps and foreign exchange forwards to commercial customers. Offsetting swap and forward agreements are simultaneously transacted to effectively eliminate the Company's market risk associated with the customer derivative products. The assets and liabilities for derivatives not designated as hedges reflect the market value of these transactions.

The table below presents RBS Citizens' derivative assets and liabilities. See further discussion of the Company's derivative instruments in the Consolidated Financial Statements.

(dollars in millions)	December 31, 2013 Notional Amount[1]	December 31, 2013 Derivative Assets	December 31, 2013 Derivative Liabilities	December 31, 2012 Notional Amount[1]	December 31, 2012 Derivative Assets	December 31, 2012 Derivative Liabilities	Net Increase (Decrease) in Net Assets/ Liabilities
Derivatives designated as hedging instruments:							
Interest rate swaps	$5,500	$23	$412	$4,200	$1	$257	52%
Derivatives not designated as hedging instruments:							
Interest rate swaps	29,355	654	558	31,227	1,102	1,033	39
Foreign exchange contracts	7,771	94	87	5,978	71	67	75
Other contracts	569	7	10	2,815	35	15	(115)
Total derivatives not designated as hedging instruments		755	655		1,208	1,115	8
Gross derivative fair values		$778	$1,067		$1,209	$1,372	77
Less: Gross amounts offset in the Consolidated Balance Sheets[2]		(128)	(128)		(54)	(54)	
Total net derivative fair values presented in the Consolidated Balance Sheets[3]		$650	$939		$1,155	$1,318	

[1] The notional or contractual amount of interest rate derivatives and foreign exchange contracts is the amount upon which interest and other payments under the contract are based. For interest rate derivatives, the notional amount is typically not exchanged. Therefore, notional amounts should not be taken as the measure of credit or market risk as they tend to greatly overstate the true economic risk of these contracts.

[2] Amounts represent the impact of legally enforceable master netting agreements that allow the Company to settle positive and negative positions.

[3] The Company also offsets assets and liabilities associated with repurchase agreements on the Consolidated Balance Sheets. See Note 3 - Securities for further information.

CAPITAL RESOURCES

As a BHC and a FHC, RBS Citizens is subject to regulation and supervision by the Federal Reserve. The primary subsidiaries of RBS Citizens are its two insured depository institutions, RBS Citizens, N.A., a national banking association whose primary federal regulator is the OCC, and Citizens Bank of Pennsylvania, a Pennsylvania-charted savings bank regulated by the Department of Banking of the Commonwealth of Pennsylvania and supervised by the FDIC as its primary federal regulator.

Under current Basel I regulation, the Federal Reserve requires RBS Citizens to maintain minimum levels with respect to its Total Capital, Tier 1 Capital, and Leverage ratios. The minimum standards for the Total Capital ratio (the ratio of the Company's Total Risk-Based Capital, which is the sum of its Tier 1 and Tier 2 Capital as defined by Federal Reserve regulation, to total risk-weighted assets) and the Tier 1 Capital ratio (the ratio of the Company's Tier 1 Capital to total risk-weighted assets) are 8.0% and 4.0%, respectively. The minimum Tier 1 Leverage ratio (the ratio of a banking organization's Tier 1 Capital to total adjusted quarterly average assets, as defined for regulatory purposes) is 3.0% for BHCs that either have the highest supervisory rating or have implemented the Federal Reserve's risk-adjusted measure for market risk. The minimum Tier 1 Leverage ratio for all other BHCs is 4.0%, unless a different minimum is specified by the Federal Reserve.

In July 2013, the U.S. agencies approved final regulatory capital rules that implement the Basel III capital framework and certain provisions of the DFA. RBS Citizens is required to comply with these rules beginning on January 1, 2015, with certain aspects of the rules phasing in through 2018. The final rules introduce a new CET1 ratio with a minimum of 4.5%; raise the minimum for the Tier 1 Risk-Based Capital ratio from 4.0% to 6.0%; maintain the minimum for the Total Risk-Based Capital ratio at 8.0%; and set a single minimum Tier 1 Leverage ratio of 4.0% for institutions such as RBS Citizens, which are not Advanced Approaches banking organizations as defined by the U.S. agencies. Final rules raise the minima required to remain well-capitalized under the agencies' prompt corrective action framework and also require maintenance of a CCB of 2.5% above the Basel III minimum for each risk-based ratio. Maintenance of the CCB is necessary to ensure full flexibility with respect to capital distributions, including redemptions of qualifying regulatory capital, as well as payment of discretionary dividends and interest on such instruments. The rules also make changes to the definition of regulatory capital elements, under which RBS Citizens expects to take advantage of the option related to AOCI that will allow RBS Citizens to continue filtering from regulatory capital all unrealized gains and losses not related to cash flow hedges for items that are not fair-valued on the balance sheet. Lastly, the rules establish a new Standardized Approach that must be used by all banking institutions to calculate risk-weighted assets used in the denominator of all non-leverage ratios.

The table below demonstrates the strength of RBS Citizens' regulatory capital ratios as of December 31, 2013. Actual Basel I ratios and pro forma Basel III ratios, which include estimated impacts of all final rule changes released in July, remain well above current Basel I and future Basel III minima:

Regulatory Ratios as of December 31, 2013 Basel I vs. Basel III Rules

Regulatory Ratio	Basel I Ratios and Requirements			Pro Forma Basel III Ratios and Requirements (including adoption of U.S. Standardized Approach Risk-Weighted Assets)		
	Actual Basel I Ratio	Required Minimum	Well-Capitalized Minimum for Purposes of Prompt Corrective Action	Pro Forma Basel III Ratio	Required Minimum + Required Capital Conservation Buffer for Non-Leverage Ratios	Well-Capitalized Minimum for Purposes of Prompt Corrective Action
Tier 1 Capital to Risk Weighted Assets	13.5%	4%	6%	13.1%	8.5%	8%
Total Capital to Risk Weighted Assets	16.1%	8%	10%	15.7%	10.5%	10%
Tier 1 Capital to Average Total Assets (Tier 1 Leverage)	11.6%	3%	5%	11.6%	4%	5%
Common Equity Tier 1 Capital to Risk Weighted Assets	Not Applicable	Not Applicable	Not Applicable	13.1%	7%	6.5%

In addition, as a foreign-owned entity, RBS Citizens would be subject to regulation proposed in the Enhanced Prudential Standards and Early Remediation Requirements for Foreign Banking Organizations and Foreign Nonbank Financial Companies, published by the Federal Reserve in December 2012. This notice of proposed rule-making would require any large foreign banking organization with consolidated U.S. assets of $50 billion or more to establish a top-tier U.S. Intermediate Holding Company over all of its bank and non-bank subsidiaries domiciled in the U.S. Under this proposal, RBS Citizens and other U.S. subsidiaries of RBS Group would join in a formal legal entity, subject to the same risk-based capital and leverage capital rules applicable to other large U.S. bank holding companies regulated by the Federal Reserve, including enhanced liquidity, single-counterparty credit limits, stress testing, early remediation, and overall risk management requirements.

RBS Citizens' assessment of capital adequacy begins with the Company's risk appetite and risk management framework, which provides for the identification, measurement and management of material risks. Required capital is determined for actual / forecasted risk portfolios using applicable regulatory capital methodologies, including estimated impacts of approved and proposed regulatory changes that will or may apply to future periods. Key analytical frameworks, which enable the comprehensive assessment of capital adequacy versus unexpected loss, supplement RBS Citizens' base case forecast. These supplemental frameworks include IST, as well as an ICAR that builds on internally-assessed EC requirements. RBS Citizens' capital planning process is supported by a robust governance framework. This process includes: 1) capital management policies and procedures, which document capital adequacy metrics and limits as well as RBS Citizens' comprehensive capital contingency plan, and 2) the active engagement of both the legal-entity boards and senior management in oversight and decision-making.

Assessment of capital adequacy for RBS Citizens and for its subsidiary banks feed development of capital plans that are submitted to the Federal Reserve as well as bank regulators. RBS Citizens prepares these plans in full compliance with the Capital Plan Rule and also participates in the Federal Reserve's annual CCAR process. Both the consolidated entity and its subsidiary banks also participate in semi-annual stress tests required by the DFA. Within this regulatory framework, RBS Citizens may only execute capital actions in accordance with a capital plan that the Federal Reserve has reviewed and to which the Federal Reserve has not objected.

RBS Citizens continues to execute against its 2013 Capital Plan, which by regulatory definition includes target capital actions through the first quarter of 2014. During 2013, RBS Citizens has completed the following capital actions:

- Paid common dividends of $55 million, $50 million and $40 million in the second, third and fourth quarter of 2013, respectively. These were in addition to $40 million common dividends paid in the first quarter of 2013 as part of the previous capital plan;

- Redeemed $289 million of floating rate junior subordinated deferrable interest debentures due March 4, 2034 from a special purpose subsidiary, which caused the redemption of $280 million of Trust Preferred Securities from RBS in the second quarter of 2013;

- Through its CBPA subsidiary, redeemed $10 million of floating rate junior subordinated deferrable interest debentures due April 22, 2032, which caused redemption of $10 million of Trust Preferred Securities from third parties in the fourth quarter of 2013;

- Paid a special common dividend of $333 million and issued $333 million of 10-year subordinated debt (the 5.158% fixed-to-floating callable subordinated debt due June 29, 2023) to RBS in the second quarter of 2013 ("Q2 exchange transaction");

- Paid a special common dividend of $333 million to RBS and issued $333 million of 10-year subordinated debt (the 4.771% fixed subordinated debt due October 1, 2023) to RBSG in the third quarter of 2013 ("Q3 exchange transaction");

- Paid a special common dividend of $334 million to RBS and issued $334 million of 10-year subordinated debt (the 4.691% fixed subordinated debt due January 2, 2024) to RBSG in the fourth quarter of 2013 ("Q4 exchange transaction").

The final three actions, which aggregate to $1 billion of "exchange transactions," were undertaken to normalize RBS Citizens' capital structure in relation to peer norms and minimum requirements implied by Basel III regulatory requirements, without impacting the overall level of qualifying regulatory capital. After execution of these actions, both CET1 and Tier 1 capital, calculated using Basel III definitions, approximated 83.7% of Total Capital. This share of Total Capital remains well above CET1 and Tier 1 minima of 66.7% and 81.0%, respectively, as implied for an institution that exactly meets the minimum Basel III ratio plus CCB requirement for CET1, Tier 1 and Total Capital. In addition, absolute levels for pro forma Basel III CET1 and Tier 1 Risk-Based ratios also remain strong for RBS Citizens. Both the Basel III CET1 and Basel III Tier 1 Risk-Based ratios were 13.1% as of December 31, 2013, well above their respective Basel III minima plus CCB of 7.0% and 8.5%, respectively. Exchanging common equity for the same amount of Tier 2 subordinated debt has no impact on either the level of Total Capital or the Total Risk-Based Capital ratio. RBS Citizens' pro forma Basel III Total Risk-Based Capital ratio after taking into effect all Basel III impacts also remained strong at 15.7% versus the Basel III minimum plus CCB of 10.5%.

As a result of the goodwill impairment recognized by RBS Citizens, N.A. in the second quarter of 2013, the national bank must request specific approval from the OCC before executing capital distributions to its parent, RBS Citizens. This requirement will be in place through the fourth quarter of 2015. Regardless of the OCC's decision regarding capital distributions by the national bank, the stand-alone BHC, as of December 31, 2013, has liquid assets in excess of $554 million compared to an annual interest burden on existing sub-debt of approximately $63 million.

CRITICAL ACCOUNTING ESTIMATES

RBS Citizens' Consolidated Financial Statements are prepared in accordance with U.S. GAAP. The preparation of financial statements in conformity with U.S. GAAP requires RBS Citizens to establish accounting policies and make estimates that affect amounts reported in the Company's Consolidated Financial Statements. The Significant Accounting Policies Note to the Consolidated Financial Statements, which is incorporated by reference into this MD&A, describes the significant accounting policies used in the Consolidated Financial Statements.

An accounting estimate requires assumptions and judgments about uncertain matters that could have a material effect on the Consolidated Financial Statements. Estimates are made using facts and circumstances known at a point in time, and changes in those facts and circumstances could produce results substantially different from those estimates. The most significant accounting policies and estimates and their related application are discussed below.

Allowance for Credit Losses

Management's estimate of probable losses in the Company's loan and lease portfolios is recorded in the ALLL and the reserve for unfunded lending commitments. The Company evaluates the adequacy of the ALLL by performing reviews of certain individual loans and leases, analyzing changes in the composition, size and delinquency of the portfolio, reviewing previous loss experience, and considering current and anticipated economic factors. The ALLL is established in accordance with Company's credit reserve policies, as approved by the Audit Committee of the Board of Directors. The Chief Financial Officer and Chief Risk Officer review the adequacy of the ALLL each quarter, together with risk management. The allowance is maintained at a level which management considers to be adequate based on the results of this evaluation, and is established through charges to earnings in the form of a provision for credit losses. Amounts determined to be uncollectible are deducted from the allowance and subsequent recoveries, if any, are added to the allowance. While management uses available information to estimate loan and lease losses, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for credit losses.

For non-impaired commercial and commercial real estate loans, the Company estimates the appropriate level of the ALLL by applying expected loss rates to existing loans with similar risk characteristics. Probable losses for commercial and commercial real estate loans are determined using a model that utilizes the probability of default, loss given default, and exposure at default on an individual loan basis. These factors consider the internal risk rating, loan tenor, and weighted average life.

For non-impaired retail loans, the ALLL is based upon the appropriate selection of either (a) losses estimated using delinquency roll rate models or (b) an expected loss model utilizing the probability of default, loss given default, and exposure at default on an individual loan basis. When developing these factors, the Company may consider the loan product and collateral type, LTV ratio, lien position, borrower's credit, time outstanding, geographic location, delinquency status, and loss emergence period. Certain retail portfolios, including SBO home equity loans, student loans, and commercial credit card receivables utilize roll rate models exclusively to estimate the ALLL. Selection of the appropriate use of delinquency roll rate or expected loss models by product is determined quarterly.

For nonaccruing commercial and commercial real estate loans with an outstanding balance of $3 million or greater and for all commercial and commercial real estate TDRs (regardless of size), the Company conducts further analysis to determine the probable amount of loss and establishes a specific allowance for the loan, if appropriate. The Company estimates the impairment amount by comparing the loan's carrying amount to the estimated present value of its future cash flows, the fair value of its underlying collateral, or the loan's observable market price. For collateral-dependent impaired commercial and commercial real estate loans, the excess of the Company's recorded investment in the loan over the fair value of the collateral less cost to sell is charged off to the ALLL.

For retail TDRs that are not collateral-dependent, allowances are developed using the present value of expected future cash flows, compared to the recorded investment in the loans. Expected re-default factors are considered in this analysis. Retail TDRs which are deemed collateral-dependent are written down to fair market value less cost to sell. The fair value of collateral is periodically monitored subsequent to the modification.

The ALLL may be adjusted to reflect the Company's current assessment of various qualitative risks, factors and events that may not be measured in the statistical analysis. Such factors include trends in economic conditions, loan growth, back testing results, base versus stress losses, credit underwriting policy exceptions, regulatory and audit findings, and peer comparisons.

In addition to the ALLL, the Company also estimates probable credit losses associated with off balance sheet financial instruments such as standby letters of credit, financial guarantees and binding unfunded loan commitments. Off balance sheet financial instruments are subject to individual reviews and are analyzed and segregated by risk according to the Company's internal risk rating scale. These risk classifications, in conjunction with historical loss experience, economic conditions and performance trends within specific portfolio segments, result in the estimate of the reserve for unfunded lending commitments.

The ALLL and the reserve for unfunded lending commitments are reported on the Consolidated Balance Sheets in the ALLL and in other liabilities, respectively. Provision for credit losses related to the loans and leases portfolio and the unfunded lending commitments are reported in the Consolidated Statements of Operations as provision for credit losses.

Commercial loans and leases are charged off to the ALLL when there is little prospect of collecting either principal or interest. Charge-offs of commercial loans and leases usually involve receipt of borrower-specific adverse information. For commercial collateral-dependent loans, an appraisal or other valuation is used to quantify a shortfall between the fair value of the collateral less costs to sell and the recorded investment in the commercial loan. Retail loan charge-offs are generally based on established delinquency thresholds rather than borrower-specific adverse information. When a loan is collateral-dependent, any shortfalls between the fair value of the collateral less costs to sell and the recorded investment is promptly charged off. Placing any loan or lease on nonaccrual status does not by itself require a partial or total charge-off; however, any identified losses are charged off at that time.

Additional information regarding RBS Citizens' allowance for credit losses can be found in the Notes to the Consolidated Financial Statements.

Nonperforming Loans and Leases

Commercial loans, commercial real estate loans, and leases are generally placed on nonaccrual status when contractually past due 90 days or more, or earlier if management believes that the probability of collection is insufficient to warrant further accrual. Some of these loans and leases may remain on accrual status when contractually past due 90 days or more if management considers the loan collectible. A loan may be returned to accrual status if (1) principal and interest payments have been brought current, and the Company expects repayment of the remaining contractual principal and interest, (2) the loan or lease has otherwise become well-secured and in the process of collection, or (3) the borrower has been making regularly scheduled payments in full for the prior six months and it's reasonably assured that the loan or lease will be brought fully current within a reasonable period. Cash receipts on nonaccruing loans and leases are generally applied to reduce the unpaid principal balance.

Residential mortgages are generally placed on nonaccrual status when past due 120 days, or sooner if determined to be collateral-dependent. Residential mortgages are returned to accrual status when principal and interest payments become less than 120 days past due and when future payments are reasonably assured. Credit card balances (included in the "unsecured" retail class of loans) are placed on nonaccrual status when past due 90 days or more. Credit card balances are restored to accruing status if they subsequently become less than 90 days past due. Guaranteed student loans (included in the "unsecured" class of loans) are not placed on nonaccrual status.

All other retail loans are generally placed on nonaccrual status when past due 90 days or more, or earlier if management believes that the probability of collection is insufficient to warrant further accrual. Loans less than 90 days past due may be placed on nonaccrual status upon the death of the borrower, surrender or repossession of collateral, fraud or bankruptcy. Loans are generally returned to accrual status if the loan becomes less than 15 days past due. Cash receipts on nonaccruing loans and leases are generally applied to reduce the unpaid principal balance. Certain TDRs that are current in payment status are classified as nonaccrual in accordance with regulatory guidance. Income on these loans is generally recognized on a cash basis if management believes that the remaining book value of the loan is realizable. Nonaccruing TDRs that meet the guidelines above for accrual status can be returned to accruing if supported by a well documented evaluation of the borrowers financial condition, and if they have been current for at least 6 months.

Additional information regarding RBS Citizens' nonperforming loans and leases can be found in the Notes to the Consolidated Financial Statements.

Impaired Loans

A loan is considered to be impaired when it is probable that the Company will be unable to collect all of the contractual interest and principal payments as scheduled in the loan agreement. Impaired loans include nonaccruing larger balance (greater than $3 million carrying value) non-homogenous commercial and commercial real estate loans, and restructured loans which are deemed TDRs. A loan modification is identified as a TDR when the Company, or bankruptcy court, grants the borrower a concession that the Company would not otherwise make in response to the borrower's financial difficulties. Concessions granted in TDRs for all classes of loans may include lowering the interest rate, forgiving a portion of principal, extending the loan term, lowering scheduled payments for a specified period of time, principal forbearance, or capitalizing past due amounts. A rate increase can be a concession if the increased rate is lower than a market rate for debt with risk similar to that of the restructured loan. Additionally, TDRs for commercial loans may also involve creating a multiple note structure, accepting non-cash assets, accepting an equity interest, or receiving a performance-based fee. In some cases a TDR may involve multiple concessions. The financial effects of TDRs for all loan classes may include lower income (either due to a lower interest rate or a delay in the timing of cash flows), larger loan loss provisions, and accelerated charge-offs if the modification renders the loan collateral-dependent. In some cases interest income throughout the term of the loan may increase if, for example, the loan is extended or the interest rate is increased as a result of the restructuring.

Impairment evaluations are performed at the individual loan level, and consider expected future cash flows from the loan, including, if appropriate, the realizable value of collateral. Impaired loans which are not TDRs are nonaccruing, and loans involved in TDRs may be accruing or nonaccruing. Retail loans that were discharged in bankruptcy and not reaffirmed by the customer are deemed to be collateral-dependent TDRs and are charged off to the fair value of the collateral, less cost to sell, and less amounts recoverable under a government guarantee (if any). Cash receipts on nonaccruing impaired loans, including nonaccruing loans involved in TDRs, are generally applied to reduce the unpaid principal balance. Certain TDRs that are current in payment status are classified as nonaccrual in accordance with regulatory guidance. Income on the loans is generally recognized on a cash basis if management believes that the remaining book value of the loan is realizable.

Loans are generally restored to accrual status when principal and interest payments are brought current and when future payments are reasonably assured, following a sustained period of repayment performance by the borrower in accordance with the loan's contractual terms.

Additional information regarding RBS Citizens' impaired loans can be found in the Notes to the Consolidated Financial Statements.

Fair Value

The Company measures fair value using the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is based upon quoted market prices in an active market, where available. If quoted prices are not available, observable market-based inputs or independently-sourced parameters are used to develop fair value, whenever possible. Such inputs may include prices of similar assets or liabilities, yield curves, interest rates, prepayment speeds, and foreign exchange rates.

A portion of the Company's assets and liabilities is carried at fair value, including AFS securities, private equity investments, and derivative instruments. In addition, the Company elects to account for its residential mortgages held for sale at fair value. The Company classifies its assets and liabilities that are carried at fair value in accordance with the three-level valuation hierarchy:

- Level 1. Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar instruments; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by market data for substantially the full term of the asset or liability.
- Level 3. Unobservable inputs that are supported by little or no market information and that are significant to the fair value measurement.

Classification in the hierarchy is based upon the lowest level input that is significant to the fair value measurement of the asset or liability. For instruments classified in Level 1 and 2 where inputs are primarily based upon observable market data, there is less judgment applied in arriving at the fair value. For instruments classified in Level 3, management judgment is more significant due to the lack of observable market data.

The Company reviews and updates the fair value hierarchy classifications on a quarterly basis. Changes from one quarter to the next related to the observability of inputs in fair value measurements may result in a reclassification between the fair value hierarchy levels and are recognized based on period-end balances.

Fair value is also used on a nonrecurring basis to evaluate certain assets for impairment or for disclosure purposes. Examples of nonrecurring uses of fair value include MSRs accounted for by the amortization method, loan impairments for certain loans, and goodwill.

Additional information regarding RBS Citizens' fair value measurements can be found in the Notes to the Consolidated Financial Statements.

Goodwill

Goodwill is not amortized, but is subject to annual impairment tests. Goodwill is assigned to reporting units at the date the goodwill is initially recorded. A reporting unit is a business operating segment or a component of a business operating segment. Once goodwill has been assigned to reporting units, it no longer retains its association with a particular acquisition, and all of the activities within a reporting unit, whether acquired or organically grown, are available to support the value of the goodwill.

The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit's fair value to its carrying value including goodwill. If the fair value of a reporting unit exceeds its carrying value, applicable goodwill is deemed to be not impaired. If the carrying value exceeds fair value, there is an indication of impairment and the second step is performed to measure the amount of impairment.

The second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination, which is the excess of the fair value of the reporting unit, as determined in the first step, over the aggregate fair values of the individual assets, liabilities and identifiable intangible assets as if the reporting unit were being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss recognized cannot exceed the amount of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted.

In September 2013, the Company changed its annual goodwill impairment test date from September 30 to October 31. The Company reviews goodwill for impairment annually as of October 31, or more often if events or circumstances indicate that it is more likely than not that the fair value of one or more reporting units is below its carrying value. The fair values of the Company's reporting units are determined using a combination of income and market-based approaches. The Company relies on the income approach (discounted cash flow method) for determining fair value. Market and transaction approaches are used as benchmarks only to corroborate the value determined by the discounted cash flow method. The Company relies on several assumptions when estimating the fair value of its reporting units using the discounted cash flow method. These assumptions include the current discount rate, as well as projected loan loss, income tax and capital retention rates.

Discount rates are estimated based on the Capital Asset Pricing Model, which considers the risk-free interest rate, market risk premium, beta, and unsystematic risk and size premium adjustments specific to a particular reporting unit. The discount rates are also calibrated on the assessment of the risks related to the projected cash flows of each reporting unit. Cash flow projections include estimates for projected loan loss, income tax and capital retention rates. Multi-year financial forecasts are developed for each reporting unit by considering several key business drivers such as new business initiatives, customer retention standards, market share changes, anticipated loan and deposit growth, forward interest rates, historical performance, and industry and economic trends, among other considerations. The long-term growth rate used in determining the terminal value of each reporting unit was estimated based on management's assessment of the minimum expected terminal growth rate of each reporting unit, as well as broader economic considerations such as GDP and inflation.

The Company based its fair value estimates on assumptions it believes to be representative of assumptions that a market participant would use in valuing the reporting unit but that are unpredictable and inherently uncertain, including estimates of future growth rates and operating margins and assumptions about the overall economic climate and the competitive environment for its reporting units. There can be no assurances that future estimates and assumptions made for purposes of goodwill testing will prove accurate predictions of the future. If the assumptions regarding business plans, competitive environments or anticipated growth rates are not achieved, the Company may be required to record goodwill impairment charges in future periods.

Additional information regarding RBS Citizens' goodwill can be found in Note 8 to the Consolidated Financial Statements.

OFF BALANCE SHEET ARRANGEMENTS

The following table presents RBS Citizens' outstanding off balance sheet commitments. See further discussion of the Company's off balance sheet arrangements in the Consolidated Financial Statements.

(dollars in millions)	December 31, 2013	December 31, 2012	Increase (Decrease)
Commitment amount:			
Undrawn commitments to extend credit	$53,987	$50,507	7%
Financial standby letters of credit	2,556	3,082	(17)
Performance letters of credit	149	152	(2)
Commercial letters of credit	64	103	(38)
Marketing rights	54	57	(5)
Risk participation agreements	17	30	(43)
Residential mortgage loans sold with recourse	13	17	(24)
Total	$56,840	$53,948	5%

ENTERPRISE RISK MANAGEMENT

RBS Citizens defines risk appetite as the maximum limit of acceptable risk, beyond which the Company would be unable to achieve its strategic objectives, or would assume an unacceptable amount of risk in order to do so. RBS Citizens' risk appetite contains four main objectives (i.e., maintain capital adequacy of 7% post-stress Tier 1 common, deliver stable earnings growth, maintain stable and efficient access to funding and maintain stakeholder confidence) and their associated measures. By including the capital adequacy target of 7% post-stress Tier 1 common within the risk appetite, RBS Citizens has made an explicit linkage between the risk appetite and the capital adequacy process. The Company considers the 7% post-stress Tier 1 common requirement when reviewing both the adequacy of capital targets and the post-stress buffer. As an additional control, and in line with RBS Citizens' risk appetite, it has also implemented an earnings volatility target that requires the Company to remain profitable under severe stress events and appropriately capitalized under extreme stress events.

As a banking organization regulated under U.K. law, RBS Group exercises enterprise-wide management over all of its subsidiaries, including RBS Citizens. Therefore, RBS Citizens must also manage its risks consistent with the maximum limit of risk acceptable to RBS Group. Pursuant to a cease and desist order entered into by RBS Group with the Federal Reserve and certain state banking supervisors in 2011 (the "Cease and Desist Order"), RBS Group was required to strengthen its U.S. corporate governance structure and develop an enterprise-wide risk management program, among other requirements with respect to its U.S. operations, which include RBS Citizens.

RBS Citizens maintains a governance structure that delineates the responsibilities for risk management activities, as well as governance and oversight of those activities, by management and the Board of Directors. Board members have access to executive management and are provided frequent and periodic management updates, including reports from Risk Management, Finance and Treasury, and RBS Group Internal Audit.

Managing risk is an essential component of RBS Citizens' business. Risk identification and monitoring are key elements in overall risk management.

The following principal risks have been incorporated into RBS Citizens' risk management program, consistent with RBS Group's enterprise-wide risk management program and the governance standards imposed by the Cease and Desist Order:

Credit Risk

Credit risk represents the potential for default or loss resulting from an obligor's or counterparty's failure to meet the terms of any contract with RBS Citizens or its subsidiaries, or failure otherwise to perform as agreed. Credit risk arises from all activities where success depends on counterparty, issuer, or borrower performance.

Credit Policy administers the Credit Approval Framework that controls the underwriting and approval of new business for the Company. Risk Policy Committees govern all changes to the retail and commercial credit policies. The Credit Approval Framework vests credit authority in select individuals throughout the Company. Transactions must be approved by designated personnel and the level of approval escalates based on the size and complexity of the transaction. RBS Citizens is currently focused on streamlining and simplifying the Credit Policy and supporting procedures to improve efficiency without compromising asset quality and sound lending processes.

Credit Portfolio Management oversight resides with assigned retail and commercial credit officers who are focused on transactions and portfolio management capabilities. Concentration limits for asset classes and sectors are formally approved by the Risk Policy and Risk Concentration Committees and approved by the Chief Credit Officer. Credit officers are responsible for monitoring the performance of assigned portfolios, credit policy compliance and adherence to concentration limits. Credit officers partner with the line of business to conduct regular portfolio reviews to identify and remediate risks and to execute on risk mitigating portfolio management strategies, including decisions on sales of assets, participation levels, limit reviews on leveraged lending arrangements and watched asset reviews.

A recovery group of credit professionals is engaged in the restructuring, remediation and collection of stressed loan relationships.

RBS Citizens' Risk Architecture Center of Excellence centralizes all activities associated with the oversight of risk systems, data, analytics, and reporting. Risk Architecture manages a single, integrated roadmap of projects to enhance its risk and capital management capabilities, inclusive of key risk initiatives around the regulatory reform agenda. These include Basel III, economic capital enhancements, comprehensive capital analysis and review, stress testing and DFA compliance.

An independent model validation function delivers objective validation assessments for all models in the decision support framework.

Relationship managers are responsible for all aspects of the credit relationship including sales negotiations, profitability, underwriting, regulatory compliance, documentation, portfolio administration, and problem loan identification. Relationship managers seek to ensure that the proper probability of default and loss given default ratings are assigned to the credit at all times. Relationship management also entails oversight and liaison with other areas of RBS Citizens whenever appropriate, particularly in deteriorating scenarios. Relationship management teams may be comprised of team leaders, relationship managers, portfolio management analysts, underwriters and lending analysts. Every member of the team plays a critical role and shares a significant level of responsibility; however, the relationship manager assigned to the credit ultimately is charged with the primary credit stewardship responsibilities and accountability.

The risk analysis and reporting function within Risk Architecture acts as an independent second line of defense by aggregating, reviewing and challenging the first line of defense and reporting portfolio performance into consolidated credit risk reports which inform the board, other executives and management of overall risk trends in the loan portfolios.

Interest Rate Risk

Interest rate risk is the risk to earnings or capital arising from movement of interest rates. It arises from differences in the maturity and / or re-pricing of assets and liabilities, including the impact of interest-rate-related options embedded in bank products. The primary objectives of interest rate risk management are to identify the nature and estimate the magnitude of interest rate risk in the structural (non-trading) balance sheet, place limits on that risk reflecting risk tolerance, and then manage the risk within those limits.

All of RBS Citizens' interest rate risk measures are within current limits. RBS Citizens' structural interest rate risk position is asset-sensitive. Net interest income would benefit from rising rates, as loan assets would generally re-price upward faster than customer deposits. Adverse exposure to declining rates is limited by the low starting level of rates. The primary drivers of this adverse exposure include prepayment risk for mortgage-related assets, pricing floors on retail deposits, and rollover risk for fixed-rate assets, all of which become magnified at low interest rate levels. Given the prolonged period of low interest rates, the cumulative impact of rollover risk grows.

Liquidity Risk

Liquidity risk is defined as the risk that RBS Citizens or any of its subsidiaries / affiliates are unable to meet their contractual or potential payment obligations in a timely manner. This risk can be broken down into asset liquidity risk and funding liquidity risk. Asset liquidity risk arises when changes in the market conditions make the liquidation of certain assets difficult and substantially reduces the liquidation value of such assets. Funding liquidity risk refers to the inability of the Company to honor its payment obligations due to difficulties raising funds from counterparties and / or depositors.

RBS Citizens considers the effective and prudent management of wholesale funding and liquidity to be fundamental to the health and strength of the Company. Liquidity risk is measured and managed within approved policy guidelines as determined by the Board of Directors, the RBS Citizens Asset and Liability Management Committee and RBS Group Asset Liability Committee. The Wholesale Funding and Liquidity unit monitors various key liquidity and funding metrics for each bank and RBS Citizens on stand-alone and consolidated bases daily. Net overnight position, free securities, internal liquidity, available FHLB borrowing capacity, and total asset liquidity are calculated on a daily basis and forecasted monthly over a one-year horizon. This forecast is intended to identify emerging balance sheet trends and risks, and inform funding decisions.

The Company calculates and monitors asset liquidity as a key indicator of contingent liquidity capacity. Asset liquidity, which remains at historically high levels, is comprised primarily of unencumbered securities and unused FHLB capacity. Precautionary excess cash balances are generally maintained at the FRB. As traditional sources of wholesale funding remain relatively limited, RBS Citizens continues to maintain minimal reliance on unsecured wholesale markets, with ample liquidity due to stable deposits, and with contingent liquidity provided by high quality loan and security assets.

Market Risk

Market risk is defined as the risk of loss resulting from changes in market prices as a result of changes in rates, credit and liquidity or general economic conditions. RBS Citizens has market risk exposure to over-the-counter derivatives (including interest rate risk management products and foreign exchange swaps / forwards), its mortgage pipeline (related to secondary marketing activities) and its AFS portfolio. The mortgage pipeline and AFS portfolio fall under the direct oversight of the Asset and Liability Management Committee. Over-the-counter derivatives are generally recognized as having low levels of market risk given RBS Citizens simultaneously enters into offsetting derivative agreements with its parent RBS. Residual market risk related to over-the-counter derivatives is confined primarily to spread / basis risk and is monitored daily using the RBS Group Market Risk's Value at Risk methodology which is based on historical simulation. Other risk measures that present risk in a complementary way to establish Value at Risk are also utilized to monitor the size and nature of the market risks RBS Citizens faces. RBS Citizens enters into hedges with RBS as warranted to neutralize its residual market risk and maintain a low risk profile.

Operational Risk

This section provides an overview of Compliance and Operational Risk Management at the Company. Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events, including legal risk. Compliance risk is defined as the conduct of RBS Citizens colleagues, either towards customers or within the markets in which the Company operates, that might lead to damage to RBS Citizens arising from a breach of regulatory rules / laws or of regulators' or customers' expectations of the Company.

Operational risk represents the possibility that inadequate or failed systems and internal controls or procedures, human error, fraud or external influences such as disasters, can cause losses. RBS Citizens' risk management framework is embedded in the business through the Three Lines of Defense Model which defines responsibilities and accountabilities.

The business units (including business areas and support functions) are the First Line of Defense and are accountable for owning and managing, within a defined risk appetite, the risks which exist in their respective business areas. These include performing and maintaining risk assessments to identify and assess the material risks that arise in their area of responsibility, complying with relevant RBS Group Policies, testing and certifying the adequacy and effectiveness of their controls on a regular basis, establishing and documenting operating procedures, establishing and owning a governance structure for identifying and managing risk, and for defining and approving an appropriate risk appetite.

The Second Line of Defense includes independent monitoring and control functions accountable for owning and developing the risk and control frameworks and tools which the business uses to discharge its responsibilities. Monitoring and control functions include the management and oversight of risk, financial management and valuation, and legal and regulatory compliance. The Second Line is appropriately independent from the business and is accountable for overseeing and challenging the First Line of Defense on the effective management of its risks. Second Line of Defense accountability includes communication, training and awareness, providing expert support and advice to the business on risk management. This includes interpreting and complying with the risk policy standards and risk management framework, conducting suitable reviews to focus on ensuring First Line compliance with policies and responsibilities, providing relevant management information and escalating concerns where appropriate. The RBS Citizens Executive Risk Committee actively considers the inherent, material risks of the business / organization. This committee analyzes the risk profile and seeks confirmation that the risks are being appropriately identified, assessed and mitigated to the desired level.

RBS Citizens Internal Audit is the Third Line of Defense and provides independent assurance over the key risks to the Company, which includes an assessment of the entire control framework.

Compliance risk is the risk of material loss, liability, reputational damage, or sanctions arising from the failure to conduct business in compliance with all relevant laws, regulations, industry or ethical standards, or regulatory guidance or expectations where the Company does business. Legal risk arises from a defective transaction, claim or other event resulting in a liability or loss, failing to take appropriate measures to protect assets, change in law and breach of law or acceptable practice. RBS Citizens has established policy standards that seek to ensure RBS Citizens works within all relevant laws and regulations applicable in all jurisdictions where it does business.

Strategic Risk

Strategic risk is the current and prospective impact on earnings or capital arising from adverse business decisions, improper implementation of decisions, or lack of responsiveness to industry changes. This risk is a function of the compatibility of an organization's strategic goals, the business strategies developed to achieve those goals, the resources deployed against these goals, and the quality of implementation. The resources needed to carry out business strategies are both tangible and intangible. They include communication channels, operating systems, delivery networks, and managerial capacities and capabilities. The Company's internal characteristics must be evaluated against the impact of economic, technological, competitive, regulatory, and other environmental changes.

There is risk in the ability to deliver upon strategic initiatives in light of a slow economic recovery and a flat yield curve. However, actions have been taken to mitigate this risk by working to optimize loan pricing and maintain conservative underwriting. Moreover, the Company is growing the fee income business and the commercial loan portfolio to drive revenue while maintaining cost discipline. The Company is positioned for a rising rate environment, but at the same time seeks alternative sources of revenue in this low rate environment. The Company will continue to run-off non-core loans and focus on organic growth as well as maintain strong capital ratios. To date, the revenue and expense impact of new regulations have been mitigated; however, as new rules are implemented, the costs of compliance will impact the Company and the entire industry.

Reputational Risk

Reputational risk is the potential for loss arising from negative public opinion. RBS Citizens manages reputational risk through various policies and processes which are embedded throughout the Company. These processes are both proactive and reactive in nature and include communications and branding strategies, extensive compliance training and strong regulatory relations, liquidity and capital adequacy planning, operational process and systems monitoring, and robust incident management protocols to address issues as they arise.

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INDEPENDENT AUDITORS' REPORT

To the Board of Directors and Stockholder of
RBS Citizens Financial Group, Inc.
Providence, Rhode Island

We have audited the accompanying consolidated financial statements of RBS Citizens Financial Group, Inc. and its subsidiaries (the "Company"), which comprise the consolidated balance sheets as of December 31, 2013 and 2012, and the consolidated statements of operations, other comprehensive income (loss), changes in stockholder's equity, and cash flows for each of the three years in the period ended December 31, 2013, and the related notes to the consolidated financial statements.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audits. We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the Company's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of RBS Citizens Financial Group, Inc. and its subsidiaries as of December 31, 2013 and 2012, and the results of their operations and their cash flows for each of the three years in the period ended December 31, 2013 in accordance with accounting principles generally accepted in the United States of America.

Deloitte & Touche LLP

March 12, 2014

RBS CITIZENS FINANCIAL GROUP, INC.
CONSOLIDATED BALANCE SHEETS

(in millions, except share data)	December 31, 2013	December 31, 2012
ASSETS:		
Cash and due from banks	$2,757	$3,063
Interest-bearing deposits in banks	233	126
Federal funds sold and securities purchased under resale agreements	—	1,100
Securities available for sale, at fair value	15,995	18,356
Securities held to maturity (estimated fair value of $4,257 and $0, respectively)	4,315	—
Other investment securities	935	1,061
Loans held for sale, at fair value	176	624
Other loans held for sale	1,078	22
Loans and leases	85,859	87,248
Less: Allowance for loan and lease losses	1,221	1,255
Net loans and leases	84,638	85,993
Derivative assets	650	1,155
Premises and equipment, net	592	643
Bank-owned life insurance	1,339	1,299
Goodwill	6,876	11,311
Due from broker	446	4
Other branch assets held for sale	46	—
Other assets	2,078	2,296
TOTAL ASSETS	$122,154	$127,053
LIABILITIES AND STOCKHOLDER'S EQUITY:		
LIABILITIES:		
Deposits:		
Noninterest-bearing	$24,931	$25,931
Interest-bearing	61,972	69,217
Total deposits	86,903	95,148
Deposits held for sale	5,277	—
Federal funds purchased and securities sold under agreements to repurchase	4,791	3,601
Short-term borrowed funds	2,251	501
Derivative liabilities	939	1,318
Deferred taxes, net	199	446
Long-term borrowed funds	1,405	694
Other liabilities	1,193	1,216
TOTAL LIABILITIES	102,958	102,924
Commitments and contingent liabilities (refer to Note 16)		
STOCKHOLDER'S EQUITY:		
Preferred stock:		
$1.00 par value, 30,000 shares authorized, no shares outstanding at December 31, 2013 and 2012	—	—
Common stock:		
$.01 par value, 5,000 shares authorized, 3,382 shares issued and outstanding at December 31, 2013 and 2012	—	—
Additional paid-in capital	18,609	18,595
Retained earnings	1,235	5,846
Accumulated other comprehensive loss	(648)	(312)
TOTAL STOCKHOLDER'S EQUITY	19,196	24,129
TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY	$122,154	$127,053

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

RBS CITIZENS FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended December 31,		
(in millions)	**2013**	**2012**	**2011**
INTEREST INCOME:			
Interest and fees on loans and leases	$3,001	$3,205	$3,434
Interest and fees on loans held for sale	12	17	13
Investment securities	477	620	750
Interest-bearing deposits in banks	11	4	7
Total interest income	3,501	3,846	4,204
INTEREST EXPENSE:			
Deposits	216	375	490
Federal funds purchased and securities sold under agreement to repurchase	192	119	191
Short-term borrowed funds	4	101	150
Long-term borrowed funds	31	24	53
Total interest expense	443	619	884
Net interest income	3,058	3,227	3,320
Provision for credit losses	479	413	882
Net interest income after provision for credit losses	2,579	2,814	2,438
NONINTEREST INCOME:			
Service charges on deposits	505	558	597
ATM and debit card	160	169	267
Mortgage banking	153	189	62
Trust and investment services revenue	149	131	131
Net gains on sales of securities available for sale	144	95	162
Other service fee income	135	146	145
International fees	97	105	114
Credit card fees	74	80	77
Capital markets income	53	52	40
Bank-owned life insurance	50	51	49
Other-than-temporary impairment:			
Total other-than-temporary impairment losses	(49)	(84)	(189)
Portions of loss recognized in other comprehensive income (before taxes)	41	60	170
Net impairment losses recognized in earnings	(8)	(24)	(19)
Other net gains	3	41	10
Other income	117	74	76
Total noninterest income	1,632	1,667	1,711
NONINTEREST EXPENSE:			
Salaries and employee benefits	1,652	1,743	1,623
Outside services	360	339	340
Occupancy	327	310	372
Equipment expense	275	279	301
Amortization of software	102	77	53
Deposit insurance	85	98	117
Promotional expense	76	86	102
Operating losses	60	196	32
Goodwill impairment	4,435	—	—
Other operating expense	307	329	431
Total noninterest expense	7,679	3,457	3,371
Income (loss) before income tax (benefit) expense	(3,468)	1,024	778
Income tax (benefit) expense	(42)	381	272
NET (LOSS) INCOME	($3,426)	$643	$506

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

RBS CITIZENS FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF OTHER COMPREHENSIVE INCOME (LOSS)

	Years Ended December 31,		
(in millions)	**2013**	**2012**	**2011**
Net (loss) income	($3,426)	$643	$506
Other comprehensive income (loss):			
Net unrealized derivative instrument gains (losses) arising during the period, net of income taxes of ($100), ($15), and ($64), respectively	(172)	(26)	(112)
Reclassification adjustment for net derivative (gains) losses included in net income, net of income taxes of $66, $123, and $188, respectively	114	212	328
Net unrealized securities (losses) gains arising during the period, net of income taxes of ($165), $80, and $163, respectively	(285)	138	286
Other than temporary impairment not recognized in earnings on securities, net of income taxes of ($15), ($22), and ($62), respectively	(26)	(38)	(108)
Reclassification of net securities gains to net income, net of income taxes of ($50), ($26), and ($52), respectively	(86)	(45)	(90)
Defined benefit pension plans:			
Actuarial gain (loss), net of taxes of $66, ($63), and ($92), respectively	110	(107)	(150)
Amortization of actuarial loss, net of taxes of $5, $14, and $8, respectively	9	24	12
Settlement/curtailment, net of taxes of $0, $34, and $0, respectively	—	58	(3)
Total other comprehensive (loss) income, net of income taxes	(336)	216	163
Total comprehensive (loss) income	($3,762)	$859	$669

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

RBS CITIZENS FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY

(in millions)	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
Balance at January 1, 2011	$0	$0	$18,538	$4,847	($691)	$22,694
Capital contribution	—	—	30	—	—	30
Comprehensive income:						
Net income	—	—	—	506	—	506
Other comprehensive income	—	—	—	—	163	163
Balance at December 31, 2011	—	—	18,568	5,353	(528)	23,393
Dividend to parent	—	—	—	(150)	—	(150)
Capital contribution	—	—	27	—	—	27
Comprehensive income:						
Net income	—	—	—	643	—	643
Other comprehensive income	—	—	—	—	216	216
Balance at December 31, 2012	—	—	18,595	5,846	(312)	24,129
Dividends to parent	—	—	—	(185)	—	(185)
Dividends to parent - exchange transactions	—	—	—	(1,000)	—	(1,000)
Capital contribution	—	—	14	—	—	14
Comprehensive income:						
Net loss	—	—	—	(3,426)	—	(3,426)
Other comprehensive loss	—	—	—	—	(336)	(336)
Balance at December 31, 2013	$0	$0	$18,609	$1,235	($648)	$19,196

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

RBS CITIZENS FINANCIAL GROUP, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended December 31,		
(in millions)	**2013**	**2012**	**2011**
OPERATING ACTIVITIES			
Net (loss) income	($3,426)	$643	$506
Adjustments to reconcile net income to net cash provided by operating activities:			
Provision for credit losses	479	413	882
Originations of mortgage loans held for sale	(3,781)	(5,496)	(3,823)
Proceeds from sales of mortgage loans held for sale	4,229	5,436	3,975
Amortization of terminated cash flow hedges	73	97	139
Depreciation, amortization and accretion	404	467	434
(Recovery) impairment of mortgage servicing rights	(47)	12	42
Securities impairment	8	24	19
Goodwill impairment	4,435	—	—
Gain on other investment securities	—	(3)	(9)
Deferred income taxes	(53)	306	252
Loss on disposal / impairment of premises and equipment	16	11	8
(Gain) loss on sales of:			
Securities available for sale	(144)	(93)	(162)
Other investment securities	—	(63)	—
Subsidiary	—	—	(7)
Premises and equipment	—	—	(2)
Other assets	—	24	—
(Increase) decrease in other assets	827	76	(164)
(Decrease) increase in other liabilities	(371)	(140)	389
Net cash provided by operating activities	2,649	1,714	2,479
INVESTING ACTIVITIES			
Investment securities:			
Purchases of securities available for sale	(10,999)	(5,532)	(13,749)
Proceeds from maturities and paydowns of securities available for sale	4,708	6,667	6,639
Proceeds from sales of securities available for sale	3,645	2,724	5,077
Purchases of other investment securities	(1)	(1)	(33)
Proceeds from sales of other investment securities	127	204	93
Purchases of securities held to maturity	(224)	—	—
Proceeds from maturities and paydowns of securities held to maturity	22	—	—
Net decrease (increase) in interest-bearing deposits in banks	993	(995)	(68)
Net decrease in cash collateral	—	—	1,485
Net increase in loans and leases	(341)	(1,432)	(1,072)
Net increase in bank-owned life insurance	(40)	(42)	(43)
Net cash payments for divestiture activities	—	(309)	—
Premises and equipment:			
Purchases	(160)	(178)	(106)
Proceeds from sales	25	6	5
Purchases of software	(208)	(193)	(262)
Net cash (used in) provided by investing activities	(2,453)	919	(2,034)
FINANCING ACTIVITIES			
Net (decrease) increase in deposits	(2,968)	2,584	733
Net increase (decrease) in federal funds purchased and securities sold under agreements to repurchase	1,190	(551)	(960)
Net change in short-term borrowed funds	1,750	(2,599)	1,662
Proceeds from long-term borrowed funds	1,002	337	9
Repayments of long-term borrowed funds	(291)	(2,885)	(3,113)
Dividends paid to parent	(1,185)	(150)	—
Net cash used in financing activities	(502)	(3,264)	(1,669)
Decrease in cash and cash equivalents	(306)	(631)	(1,224)
Cash and cash equivalents at beginning of year	3,063	3,694	4,918
Cash and cash equivalents at end of year	$2,757	$3,063	$3,694

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

NOTE 1 - SIGNIFICANT ACCOUNTING POLICIES

The accounting and reporting policies of RBS Citizens conform to U.S. GAAP. The Company is a wholly-owned subsidiary of The Royal Bank of Scotland plc, a banking subsidiary of the ultimate parent, The Royal Bank of Scotland Group plc. On December 1, 2008, the UK Government became the ultimate controlling party of RBSG. The UK Government's shareholding is managed by UK Financial Investments Limited, a Company wholly owned by the UK Government. The Company's principal business activity is banking, conducted through its subsidiaries RBS Citizens, N.A. and Citizens Bank of Pennsylvania.

Following is a summary of the significant accounting policies of the Company:

Basis of Presentation

The Consolidated Financial Statements include the accounts of the Company. All intercompany transactions and balances have been eliminated. The Company has evaluated its unconsolidated entities and does not believe that any entity in which it has an interest, but does not currently consolidate, meets the requirements for a variable interest entity to be consolidated.

The preparation of financial statements in conformity with U.S. GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Material estimates that are particularly susceptible to significant change in the near term relate to the determination of the provision for credit losses, evaluation and measurement of impairment of goodwill, evaluation of unrealized losses on securities for other-than-temporary impairment, accounting for income taxes, the valuation of AFS and HTM securities, and derivatives.

Cash and Cash Equivalents

For the purposes of reporting cash flows, cash and cash equivalents includes cash and due from banks.

Interest-Bearing Deposits in Banks

Interest-bearing deposits in banks are carried at cost and include deposits that mature within one year.

Securities

Investments in debt and equity securities are carried in four portfolios: AFS, HTM, trading account assets and other investment securities. Management determines the appropriate classification at the time of purchase.

Securities in the AFS portfolio will be held for indefinite periods of time and may be sold in response to changes in interest rates, changes in prepayment risk, or other factors in managing the Company's asset / liability strategy. Gains and losses on the sales of securities are recognized in earnings and are computed using the specific identification method. Security impairments (i.e. declines in the fair value of securities below cost) that are considered by management to be other-than-temporary are recognized in earnings as realized losses. However, the determination of the impairment amount is dependent on the Company's intent to sell (or not sell) the security. If the Company intends to sell the impaired security, the impairment loss recognized in current period earnings equals the difference between the instrument's fair value and amortized cost. If the Company does not intend to sell the impaired security, and it is not likely that the Company will be required to sell the impaired security, the credit-related impairment loss is recognized in current period earnings and equals the difference between the amortized cost of the security and the present value of the expected cash flows that have currently been projected.

Securities AFS are carried at fair value, with unrealized gains and losses reported in OCI as a separate component of stockholder's equity, net of taxes. Premiums and discounts on debt securities are amortized or accreted using a level-yield method over the estimated lives of the individual securities. The Company uses actual prepayment experience and estimates of future prepayments to determine the constant effective yield necessary to apply the interest method of income recognition. Estimates of future prepayments are based on the underlying collateral characteristics of each security and are derived from market sources. Judgment is involved in making determinations about prepayment expectations and in changing those expectations in response to changes in interest rates and macroeconomic conditions. The amortization of premiums and discounts associated with mortgage-backed securities may be significantly impacted by changes in prepayment assumptions.

Securities are classified as HTM because the Company has the ability and intent to hold the securities to maturity. Transfers of debt securities into the HTM category from the AFS category are made at fair value at the date of transfer. The unrealized holding gain or loss at the date of transfer is retained in Other Comprehensive Income and in the carrying value of the HTM securities. Such amounts are amortized over the remaining life of the security. The securities are reported at cost, adjusted for amortization of premium and accretion of discount. Interest income is recorded on the accrual basis adjusted for the amortization of premium and the accretion of discount.

Trading account assets are comprised of debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading account assets and are carried at fair value. Realized and unrealized gains and losses on such assets are reported in noninterest income in the Consolidated Statements of Operations. Trading account assets are reported in other assets in the Consolidated Balance Sheets.

Other investment securities are comprised mainly of FHLB stock and FRB stock, which are carried at cost; and venture capital investments, which are carried at fair value, with changes in fair value recognized in noninterest income. For securities that are not publicly traded, estimates of fair value are made based upon review of the investee's financial results, condition and prospects. Other investment securities, which are carried at cost, are reviewed at least annually for impairment, with valuation adjustments recognized in noninterest income.

Loans and Leases

Loans are reported at the amount of their outstanding principal, net of charge-offs, unearned income, deferred loan origination fees and costs, and unamortized premiums or discounts (on purchased loans). Deferred loan origination fees and costs and purchase discounts and premiums are amortized as an adjustment of yield over the life of the loan, using the level yield interest method. Unamortized amounts remaining upon prepayment or sale are recorded as interest income or gain (loss) on sale, respectively. Credit card receivables include billed and uncollected interest and fees.

Leases are classified at the inception of the lease. Lease receivables, including leveraged leases, are reported at the aggregate of lease payments receivable and estimated residual values, net of unearned and deferred income, including unamortized investment credits. Lease residual values are reviewed at least annually for other-than-temporary impairment, with valuation adjustments recognized currently against noninterest income. Leveraged leases are reported net of non-recourse debt. Unearned income is recognized to yield a level rate of return on the net investment in the leases.

Loans and leases are disclosed in portfolio segments and classes. The Company's loan and lease portfolio segments are commercial and retail. The classes of loans and leases are: commercial, commercial real estate, leases, residential (includes residential mortgages and home equity loans and lines of credit), home equity products serviced by others (includes certain purchased home equity loans and lines of credit), other secured retail (includes automobile loans and other installment loans), and unsecured retail (includes student loans and credit card).

Loans held for sale are carried at the lower of cost or fair value.

Allowance for Credit Losses

Management's estimate of probable losses in the Company's loan and lease portfolios is recorded in the ALLL and the reserve for unfunded lending commitments. The Company evaluates the adequacy of the ALLL by performing reviews of certain individual loans and leases, analyzing changes in the composition, size and delinquency of the portfolio, reviewing previous loss experience, and considering current and anticipated economic factors. The ALLL is established in accordance with Company's credit reserve policies, as approved by the Audit Committee of the Board of Directors. The Chief Financial Officer and Chief Risk Officer review the adequacy of the ALLL each quarter, together with risk management. The ALLL is maintained at a level which management considers to be adequate based on the results of this evaluation, and is established through charges to earnings in the form of a provision for credit losses. Amounts determined to be uncollectible are deducted from the allowance and subsequent recoveries, if any, are added to the allowance. While management uses available information to estimate loan and lease losses, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for credit losses.

For non-impaired commercial and commercial real estate loans, the Company estimates the appropriate level of the ALLL by applying expected loss rates to existing loans with similar risk characteristics. Probable losses for commercial and commercial real estate loans are determined using a model that utilizes the probability of default, loss given default, and exposure at default on an individual loan basis. These factors consider the internal risk rating, loan tenor, and weighted average life.

For non-impaired retail loans, the ALLL is based upon the appropriate selection of either (a) losses estimated using delinquency roll rate models or (b) an expected loss model utilizing the probability of default, loss given default, and exposure at default on an individual loan basis. When developing these factors, the Company may consider the loan product and collateral type, LTV ratio, lien position, borrower's credit, time outstanding, geographic location, delinquency status, and loss emergence period. Certain retail portfolios, including SBO home equity loans, student loans, and commercial credit card receivables utilize roll rate models exclusively to estimate the ALLL. Selection of the appropriate use of delinquency roll rate or expected loss models by product is determined quarterly.

For nonaccruing commercial and commercial real estate loans with an outstanding balance of $3 million or greater and for all commercial and commercial real estate TDRs (regardless of size), the Company conducts further analysis to determine the probable amount of loss and establishes a specific allowance for the loan, if appropriate. The Company estimates the impairment amount by comparing the loan's carrying amount to the estimated present value of its future cash flows, the fair value of its underlying collateral, or the loan's observable market price. For collateral-dependent impaired commercial and commercial real estate loans, the excess of the Company's recorded investment in the loan over the fair value of the collateral less cost to sell is charged off to the ALLL.

For retail TDRs that are not collateral-dependent, allowances are developed using the present value of expected future cash flows, compared to the recorded investment in the loans. Expected re-default factors are considered in this analysis. Retail TDRs which are deemed collateral-dependent are written down to fair market value less cost to sell. The fair value of collateral is periodically monitored subsequent to the modification.

The ALLL may be adjusted to reflect the Company's current assessment of various qualitative risks, factors and events that may not be measured in the statistical analysis. Such factors include trends in economic conditions, loan growth, back testing results, base versus stress losses, credit underwriting policy exceptions, regulatory and audit findings, and peer comparisons.

In addition to the ALLL, the Company also estimates probable credit losses associated with off balance sheet financial instruments such as standby letters of credit, financial guarantees and binding unfunded loan commitments. Off balance sheet financial instruments are subject to individual reviews and are analyzed and segregated by risk according to the Company's internal risk rating scale. These risk classifications, in conjunction with historical loss experience, economic conditions and performance trends within specific portfolio segments, result in the estimate of the reserve for unfunded lending commitments.

The ALLL and the reserve for unfunded lending commitments are reported on the Consolidated Balance Sheets in the ALLL and in other liabilities, respectively. Provision for credit losses related to the loans and leases portfolio and the unfunded lending commitments are reported in the Consolidated Statements of Operations as provision for credit losses.

Commercial loans and leases are charged off to the allowance when there is little prospect of collecting either principal or interest. Charge-offs of commercial loans and leases usually involve receipt of borrower-specific adverse information. For commercial collateral-dependent loans, an appraisal or other valuation is used to quantify a shortfall between the fair value of the collateral less costs to sell and the recorded investment in the commercial loan. Retail loan charge-offs are generally based on established delinquency thresholds rather than borrower-specific adverse information. When a loan is collateral-dependent, any shortfalls between the fair value of the collateral less costs to sell and the recorded investment is promptly charged off. Placing any loan or lease on nonaccrual status does not by itself require a partial or total charge-off; however, any identified losses are charged off at that time.

Nonperforming Loans and Leases

Commercial loans, commercial real estate loans, and leases are generally placed on nonaccrual status when contractually past due 90 days or more, or earlier if management believes that the probability of collection is insufficient to warrant further accrual. Some of these loans and leases may remain on accrual status when contractually past due 90 days or more if management considers the loan collectible. A loan may be returned to accrual status if (1) principal and interest payments have been brought current, and the Company expects repayment of the remaining contractual principal and interest, (2) the loan or lease has otherwise become well-secured and in the process of collection, or (3) the borrower has been making regularly scheduled payments in full for the prior six months and it's reasonably assured that the loan or lease will be brought fully current within a reasonable period. Cash receipts on nonaccruing loans and leases are generally applied to reduce the unpaid principal balance.

Residential mortgages are generally placed on nonaccrual status when past due 120 days, or sooner if determined to be collateral-dependent. Residential mortgages are returned to accrual status when principal and interest payments become less than 120 days past due and when future payments are reasonably assured. Credit card balances (included in the "unsecured" retail class of loans) are placed on nonaccrual status when past due 90 days or more. Credit card balances are restored to accruing status if they subsequently become less than 90 days past due. Guaranteed student loans (included in the "unsecured" class of loans) are not placed on nonaccrual status.

All other retail loans are generally placed on nonaccrual status when past due 90 days or more, or earlier if management believes that the probability of collection is insufficient to warrant further accrual. Loans less than 90 days past due may be placed on nonaccrual status upon the death of the borrower, surrender or repossession of collateral, fraud or bankruptcy. Loans are generally returned to accrual status if the loan becomes less than 15 days past due. Cash receipts on nonaccruing loans and leases are generally applied to reduce the unpaid principal balance. Certain TDRs that are current in payment status are classified as nonaccrual in accordance with regulatory guidance. Income on these loans is generally recognized on a cash basis if management believes that the remaining book value of the loan is realizable. Nonaccruing TDRs that meet the guidelines above for accrual status can be returned to accruing if supported by a well documented evaluation of the borrowers financial condition, and if they have been current for at least 6 months.

Impaired Loans

A loan is considered to be impaired when it is probable that the Company will be unable to collect all of the contractual interest and principal payments as scheduled in the loan agreement. Impaired loans include nonaccruing larger balance (greater than $3 million carrying value) non-homogenous commercial and commercial real estate loans, and restructured loans which are deemed TDRs. A loan modification is identified as a TDR when the Company, or bankruptcy court, grants the borrower a concession the Company would not otherwise make in response to the borrower's financial difficulties. Concessions granted in TDRs for all classes of loans may include lowering the interest rate, forgiving a portion of principal, extending the loan term, lowering scheduled payments for a specified period of time, principal forbearance, or capitalizing past due amounts. A rate increase can be a concession if the increased rate is lower than a market rate for debt with risk similar to that of the restructured loan. Additionally, TDRs for commercial loans may also involve creating a multiple note structure, accepting non-cash assets, accepting an equity interest, or receiving a performance-based fee. In some cases a TDR may involve multiple concessions. The financial effects of TDRs for all loan classes may include lower income (either due to a lower interest rate or a delay in the timing of cash flows), larger loan loss provisions, and accelerated charge-offs if the modification renders the loan collateral-dependent. In some cases interest income throughout the term of the loan may increase if, for example, the loan is extended or the interest rate is increased as a result of the restructuring.

Impairment evaluations are performed at the individual loan level, and consider expected future cash flows from the loan, including, if appropriate, the realizable value of collateral. Impaired loans which are not TDRs are nonaccruing, and loans involved in TDRs may be accruing or nonaccruing. Retail loans that were discharged in bankruptcy and not reaffirmed by the customer are deemed to be collateral-dependent TDRs and are charged off to the fair value of the collateral, less cost to sell, and less amounts recoverable under a government guarantee (if any). Cash receipts on nonaccruing impaired loans, including nonaccruing loans involved in TDRs, are generally applied to reduce the unpaid principal balance. Certain TDRs that are current in payment status are classified as nonaccrual in accordance with regulatory guidance. Income on the loans is generally recognized on a cash basis if management believes that the remaining book value of the loan is realizable.

Loans are generally restored to accrual status when principal and interest payments are brought current and when future payments are reasonably assured, following a sustained period of repayment performance by the borrower in accordance with the loan's contractual terms.

Premises and Equipment

Premises and equipment are stated at cost, less accumulated depreciation and amortization. Depreciation and amortization have been computed using the straight-line method over the estimated useful lives of the assets. Leasehold improvements are amortized over the life of the lease (including renewal options if exercise of those options is reasonably assured) or their estimated useful life, whichever is shorter.

Additions to property, plant and equipment are recorded at cost. The cost of major additions, improvements and betterments are capitalized. Normal repairs and maintenance and other costs that do not improve the property, extend the useful life or otherwise do not meet capitalization criteria are charged to expense as incurred. The Company evaluates premises and equipment for impairment when events or changes in circumstances indicate that the carrying value of such assets may not be recoverable.

Software

Costs related to computer software, developed or obtained for internal use, are capitalized if the projects improve functionality and provide long-term future operational benefits. Capitalized costs are amortized using the straight-line method over the assets expected useful life and is based upon the basic pattern of consumption and economic benefits provided by the asset. The Company begins to amortize the software when the asset (or identifiable component of the asset) is substantially complete and ready for its intended use. All other costs incurred in connection with an internal use software project are expensed as incurred. Capitalized software is included in other assets on the Consolidated Balance Sheets.

Fair Value

The Company measures fair value using the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Fair value is based upon quoted market prices in an active market, where available. If quoted prices are not available, observable market-based inputs or independently sourced parameters are used to develop fair value, whenever possible. Such inputs may include prices of similar assets or liabilities, yield curves, interest rates, prepayment speeds, and foreign exchange rates.

A portion of the Company's assets and liabilities is carried at fair value, including AFS securities, private equity investments, and derivative instruments. In addition, the Company elects to account for its residential mortgages held for sale at fair value. The Company classifies its assets and liabilities that are carried at fair value in accordance with the three-level valuation hierarchy:

- Level 1. Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2. Observable inputs other than Level 1 prices, such as quoted prices for similar instruments; quoted prices in markets that are not active; or other inputs that are observable or can be corroborated by market data for substantially the full term of the asset or liability.
- Level 3. Unobservable inputs that are supported by little or no market information and that are significant to the fair value measurement.

Classification in the hierarchy is based upon the lowest level input that is significant to the fair value measurement of the asset or liability. For instruments classified in Level 1 and 2 where inputs are primarily based upon observable market data, there is less judgment applied in arriving at the fair value. For instruments classified in Level 3, management judgment is more significant due to the lack of observable market data.

The Company reviews and updates the fair value hierarchy classifications on a quarterly basis. Changes from one quarter to the next related to the observability of inputs in fair value measurements may result in a reclassification between the fair value hierarchy levels and are recognized based on period-end balances.

Fair value is also used on a nonrecurring basis to evaluate certain assets for impairment or for disclosure purposes. Examples of nonrecurring uses of fair value include MSRs accounted for by the amortization method, loan impairments for certain loans, and goodwill.

Goodwill

Goodwill is not amortized, but is subject to annual impairment tests. Goodwill is assigned to reporting units at the date the goodwill is initially recorded. A reporting unit is a business operating segment or a component of a business operating segment. Once goodwill has been assigned to reporting units, it no longer retains its association with a particular acquisition, and all of the activities within a reporting unit, whether acquired or organically grown, are available to support the value of the goodwill.

The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit's fair value to its carrying value including goodwill. If the fair value of a reporting unit exceeds its carrying value, applicable goodwill is deemed to be not impaired. If the carrying value exceeds fair value, there is an indication of impairment and the second step is performed to measure the amount of impairment.

The second step involves calculating an implied fair value of goodwill for each reporting unit for which the first step indicated impairment. The implied fair value of goodwill is determined in the same manner as the amount of goodwill recognized in a business combination, which is the excess of the fair value of the reporting unit, as determined in the first step, over the aggregate fair values of the individual assets, liabilities and identifiable intangible assets as if the reporting unit were being acquired in a business combination. If the implied fair value of goodwill exceeds the carrying value of goodwill assigned to the reporting unit, there is no impairment. If the carrying value of goodwill assigned to a reporting unit exceeds the implied fair value of the goodwill, an impairment charge is recorded for the excess. An impairment loss recognized cannot exceed the amount of goodwill assigned to a reporting unit, and the loss establishes a new basis in the goodwill. Subsequent reversal of goodwill impairment losses is not permitted.

In September 2013, the Company changed its annual goodwill impairment test date from September 30 to October 31. The Company reviews goodwill for impairment annually as of October 31, or more often if events or circumstances indicate that it is more likely than not that the fair value of one or more reporting units is below its carrying value. The fair values of the Company's reporting units are determined using a combination of income and market-based approaches. The Company relies on the income approach (discounted cash flow method) for determining fair value. Market and transaction approaches are used as benchmarks only to corroborate the value determined by the discounted cash flow method. The Company relies on several assumptions when estimating the fair value of its reporting units using the discounted cash flow method. These assumptions include the current discount rate, as well as projected loan loss, income tax and capital retention rates.

Discount rates are estimated based on the Capital Asset Pricing Model, which considers the risk-free interest rate, market risk premium, beta, and unsystematic risk and size premium adjustments specific to a particular reporting unit. The discount rates are also calibrated on the assessment of the risks related to the projected cash flows of each reporting unit. Cash flow projections include estimates for projected loan loss, income tax and capital retention rates. Multi-year financial forecasts are developed for each reporting unit by considering several key business drivers such as new business initiatives, customer retention standards, market share changes, anticipated loan and deposit growth, forward interest rates, historical performance, and industry and economic trends, among other considerations. The long-term growth rate used in determining the terminal value of each reporting unit was estimated based on management's assessment of the minimum expected terminal growth rate of each reporting unit, as well as broader economic considerations such as GDP and inflation.

The Company based its fair value estimates on assumptions it believes to be representative of assumptions that a market participant would use in valuing the reporting unit but that are unpredictable and inherently uncertain, including estimates of future growth rates and operating margins and assumptions about the overall economic climate and the competitive environment for its reporting units. There can be no assurances that future estimates and assumptions made for purposes of goodwill testing will prove accurate predictions of the future. If the assumptions regarding business plans, competitive environments or anticipated growth rates are not achieved, the Company may be required to record goodwill impairment charges in future periods.

Bank-Owned Life Insurance

Bank-owned life insurance is stated at its cash surrender value. The Company is the beneficiary of life insurance policies on current and former officers and selected employees of the Company.

Employee Benefits

Pension costs under defined benefit plans are actuarially computed and include current service costs and amortization of prior service costs over the participants' average future working lifetime. The actuarial cost method used in determining the net periodic pension cost is the projected unit credit method. The cost of postretirement and postemployment benefits other than pensions is recognized on an accrual basis during the periods employees provide services to earn those benefits.

Derivatives

The Company is party to a variety of derivative transactions, including interest rate swap contracts, interest rate options, foreign exchange contracts, residential loan commitment rate locks, forward sale contracts, warrants and purchase options. The Company enters into contracts in order to meet the financing needs of its customers. The Company also enters into contracts as a means of reducing its interest rate and foreign currency risks and these contracts are designated as hedges when acquired based on management's intent. The Company monitors the results of each transaction to ensure that management's intent is satisfied.

All derivatives, whether designated for hedging relationships or not, are recognized in the Consolidated Balance Sheets at fair value. If a derivative is designated as a cash flow hedge, the effective portions of changes in the fair value of the derivative are recorded in accumulated OCI, a component of stockholder's equity. The ineffective portions of cash flow hedges are immediately recognized as an adjustment to income or expense. For cash flow hedging relationships that have been discontinued, balances in OCI are reclassified to interest expense in the periods during which the hedged item affects income. If it is probable that the hedged forecasted transaction will not occur, balances in OCI are reclassified immediately to income. If a derivative is designated as a fair value hedge, changes in the fair value of the derivative and the changes in the fair value of the hedged item that are due to the hedged risk are recorded in income. Changes in the fair value of derivatives that do not qualify as hedges are recognized immediately in earnings.

Derivative assets and derivative liabilities governed by master netting agreements are netted by counterparty on the balance sheet, and this netted derivative asset or liability position is also netted against the fair value of any cash collateral that has been pledged or received in accordance with a CSA.

Transfers and Servicing of Financial Assets

A transfer of financial assets is accounted for as a sale when control over the assets transferred is surrendered. Assets transferred that satisfy the conditions of a sale are derecognized, and all assets obtained and liabilities incurred in a purchase are recognized and measured at fair value. Servicing rights retained in the transfer of financial assets are initially recognized at fair value. Subsequent to the initial recognition date, the Company recognizes periodic amortization expense of servicing rights and assesses servicing rights for impairment.

Mortgage Banking

Mortgage loans held for sale are accounted for at fair value on an individual loan basis. Changes in the fair value, and realized gains and losses on the sales of mortgage loans, are reported in mortgage banking income.

The fair value of MSRs is determined based on expected future cash flows discounted at an interest rate commensurate with the servicing risks involved. MSRs are presented in the Consolidated Balance Sheets net of accumulated amortization, which is recorded in proportion to, and over the period of, net servicing income. The Company's identification of MSRs in a single class was determined based on the availability of market inputs and the Company's method of managing MSR risks. For the purpose of evaluating impairment, MSRs are stratified based on predominant risk characteristics (such as interest rate, loan size, origination date, term, or geographic location) of the underlying loans. An allowance is then established in the event the recorded value of an individual stratum exceeds fair value.

The Company determines the fair value of MSRs using a model that calculates the present value of estimated net future servicing income. The model utilizes assumptions that market participants use in estimating future net servicing income, including estimates of prepayment speeds, default rates, cost to service, discount rate, escrow earnings, contractual servicing fee income, and ancillary income. The discount rate is the required rate of return investors in the market would expect for an asset of similar risk.

The Company accounts for derivatives in its mortgage banking operations at fair value on the balance sheet as derivative assets or derivative liabilities, depending on whether the derivative had a positive (asset) or negative (liability) fair value as of the balance sheet date. The Company's mortgage banking derivatives include commitments to originate mortgages held for sale, certain loan sale agreements, and other financial instruments that meet the definition of a derivative.

Income Taxes

The Company uses an asset and liability (balance sheet) approach for financial accounting and reporting of income taxes. This results in two components of income tax expense: current and deferred. Current income tax expense approximates taxes to be paid or refunded for the current period. Deferred income tax expense results from changes in deferred tax assets and liabilities between periods. These gross deferred tax assets and liabilities represent decreases or increases in taxes expected to be paid in the future because of future reversals of temporary differences in the bases of assets and liabilities as measured by tax laws and their bases as reported in the Consolidated Financial Statements.

Deferred tax assets are recognized for net operating loss carryforwards and tax credit carryforwards. Valuation allowances are recorded as necessary to reduce deferred tax assets to the amounts management concludes are more likely than not to be realized.

The Company also assesses the probability that the positions taken or expected to be taken in its income tax returns will be sustained by taxing authorities. A "more likely than not" (more than 50 percent) recognition threshold must be met before a tax benefit can be recognized. Tax positions that are more likely than not to be sustained are reflected in the Company's Consolidated Financial Statements.

Tax positions are measured as the largest amount of tax benefit that is greater than 50 percent likely of being realized upon settlement with a taxing authority that has full knowledge of all relevant information. The difference between the benefit recognized for a position and the tax benefit claimed on a tax return is referred to as an unrecognized tax benefit.

New Accounting Pronouncements

In January 2014, the FASB issued Accounting Standards Update 2014-04, "*Reclassification of Residential Real Estate Collateralized Consumer Mortgage Loans upon Foreclosure*." This amendment clarifies that an in-substance repossession or foreclosure occurs, and a creditor is considered to have received physical possession of residential real estate property collateralizing a consumer mortgage loan, upon either (1) the creditor obtaining legal title to the residential real estate property upon completion of a foreclosure or (2) the borrower conveying all interest in the residential real estate property to the creditor to satisfy that loan through completion of a deed in lieu of foreclosure or through a similar legal agreement. The amendment require disclosure of both (1) the amount of foreclosed residential real estate property held by the creditor and (2) the recorded investment in consumer mortgage loans collateralized by residential real estate property that are in the process of foreclosure according to local requirements of the applicable jurisdiction. This amendment is effective for annual periods, and interim periods within those annual periods, beginning after December 15, 2014 and is expected to have an immaterial impact on the Company's Consolidated Financial Statements.

Also in January 2014, the FASB issued Accounting Standards Update No. 2014-01, "*Accounting for Investments in Qualified Affordable Housing Projects*." This amendment permits reporting entities to make an accounting policy election to account for their investments in qualified affordable housing projects using the proportional amortization method if certain conditions are met. Under the proportional amortization method, an entity amortizes the initial cost of the investment in proportion to the tax credits and other tax benefits received and recognizes the net investment performance in the income statement as a component of income tax expense (benefit). Qualified affordable housing project investments that are not accounted for using the proportional amortization method must be accounted for as an equity method or cost method investment. This amendment is effective for annual periods and interim reporting periods within those annual periods, beginning after December 15, 2014 and is expected to have an immaterial impact on the Company's Consolidated Financial Statements.

Reclassifications of Prior Year Amounts

Certain reclassifications were made to the prior year Financial Statements to conform to the 2013 presentation. Significant reclassifications are as follows:

- The Company reclassified student loans from the secured retail loan class to the other unsecured retail loan class.
- The Company reclassified the 2012 $75 million gain related to the sale of its Visa Inc. Class B shares from Net Gains on Securities Available for Sale to Other Net Gains on the Consolidated Statements of Operations.
- The Company reclassified software amortization from equipment expense to amortization of software on the Consolidated Statements of Operations. The software balance from 2012 was reclassified from Premises and Equipment to Other Assets in the Consolidated Balance Sheets.

NOTE 2 - CASH AND DUE FROM BANKS

The Company's subsidiary banks maintain certain average reserve balances and compensating balances for check clearing and other services with the FRB. At December 31, 2013 and 2012, the balance of deposits at the FRB amounted to $1.4 billion. Average balances maintained with the FRB during the years ended December 31, 2013, 2012, and 2011 exceeded amounts required by law for the FRB's requirements. All amounts, both required and excess reserves, held at the FRB currently earn interest at a fixed rate of 25 basis points. As a result, the Company recorded, in interest-bearing deposits in banks, interest income on FRB deposits of $5 million, $3 million, and $5 million in 2013, 2012, and 2011, respectively.

NOTE 3 - SECURITIES

The following table provides the major components of securities at amortized cost and fair value:

	December 31, 2013				December 31, 2012			
(in millions)	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
Available For Sale Securities								
U.S. Treasury	$15	$0	$0	$15	$15	$0	$0	$15
State and political subdivisions	11	—	(1)	10	20	1	—	21
Mortgage-backed securities:								
Federal agencies and U.S. government sponsored entities	14,970	151	(128)	14,993	16,368	537	(1)	16,904
Other / non-agency	992	5	(45)	952	1,452	13	(68)	1,397
Total mortgage-backed securities	15,962	156	(173)	15,945	17,820	550	(69)	18,301
Total debt securities	15,988	156	(174)	15,970	17,855	551	(69)	18,337
Marketable equity securities	10	3	—	13	5	2	—	7
Other equity securities	12	—	—	12	12	—	—	12
Total equity securities	22	3	—	25	17	2	—	19
Total available for sale securities	$16,010	$159	($174)	$15,995	$17,872	$553	($69)	$18,356
Held To Maturity Securities								
Mortgage-backed securities:								
Federal agencies and U.S. government sponsored entities	$2,940	$0	($33)	$2,907	$0	$0	$0	$0
Other / non-agency	1,375	—	(25)	1,350	—	—	—	—
Total held to maturity securities	$4,315	$0	($58)	$4,257	$0	$0	$0	$0
Other Investment Securities								
Federal Reserve Bank stock	$462	$0	$0	$462	$490	$0	$0	$490
Federal Home Loan Bank stock	468	—	—	468	565	—	—	565
Venture capital and other investments	5	—	—	5	6	—	—	6
Total other investment securities	$935	$0	$0	$935	$1,061	$0	$0	$1,061

During 2013, to reduce the growing potential negative impact of AFS securities market volatility on tangible common equity, the Company transferred a total of $4.2 billion, consisting of federal agency and other non-agency from the AFS securities portfolio to establish an HTM securities portfolio. At the time of transfer, $134 million of unrealized net losses were recognized in OCI. The amounts in OCI will be recognized in interest income over the remaining life of the securities as an offset to the adjustment of yield in a manner consistent with the amortization of premium and the accretion of discount, resulting in no impact on net income.

The Company has reviewed its securities portfolio for other-than-temporary impairments. The following tables summarize those securities whose fair values are below carrying values, segregated by those that have been in a continuous unrealized loss position for less than twelve months, and those that have been in a continuous unrealized loss position for twelve months or longer:

	December 31, 2013								
	Less than 12 Months			12 Months or Longer			Total		
(dollars in millions)	Number of Issues	Fair Value	Gross Unrealized Losses	Number of Issues	Fair Value	Gross Unrealized Losses	Number of Issues	Fair Value	Gross Unrealized Losses
State and political subdivisions	1	$10	($1)	0	$0	$0	1	$10	($1)
Mortgage-backed securities:									
Federal agencies and U.S. government sponsored entities	263	12,067	(159)	7	20	(2)	270	12,087	(161)
Other / non-agency	22	1,452	(34)	19	490	(37)	41	1,942	(71)
Total mortgage-backed securities	285	13,519	(193)	26	510	(39)	311	14,029	(232)
Total	286	$13,529	($194)	26	$510	($39)	312	$14,039	($233)

	December 31, 2012								
	Less than 12 Months			12 Months or Longer			Total		
(dollars in millions)	Number of Issues	Fair Value	Gross Unrealized Losses	Number of Issues	Fair Value	Gross Unrealized Losses	Number of Issues	Fair Value	Gross Unrealized Losses
Mortgage-backed securities:									
Federal agencies and U.S. government sponsored entities	29	$139	($1)	1	$3	$0	30	$142	($1)
Other / non-agency	2	53	(1)	29	854	(67)	31	907	(68)
Total	31	$192	($2)	30	$857	($67)	61	$1,049	($69)

For each debt security identified with an unrealized loss, the Company reviews the expected cash flows to determine if the impairment in value is temporary or other-than-temporary. If the Company has determined that the present value of the debt security's expected cash flows is less than its amortized cost basis, an other-than-temporary impairment is deemed to have occurred. The amount of impairment loss that is recognized in current period earnings is dependent on the Company's intent to sell (or not sell) the security.

If the Company intends to sell the impaired security, the impairment loss recognized in current period earnings equals the difference between the instrument's fair value and its amortized cost. If the Company does not intend to sell the impaired security, and it is not likely that the Company will be required to sell the impaired security, the credit-related impairment loss is recognized in current period earnings and equals the difference between the amortized cost of the security and the present value of the expected cash flows that have currently been projected.

In addition to these cash flow projections, several other characteristics of each security are reviewed when determining whether a credit loss exists and the period over which the debt security is expected to recover. These characteristics include: (1) the type of investment, (2) various market factors affecting the fair value of the security (e.g., interest rates, spread levels, liquidity in the sector, etc.), (3) the length and severity of impairment, and (4) the public credit rating of the instrument.

The Company estimates the portion of loss attributable to credit using a cash flow model. The inputs to this model include prepayment, default and loss severity assumptions that are based on industry research and observed data. The loss projections generated by the model are reviewed on a quarterly basis by a cross-functional governance committee. This governance committee determines whether security impairments are other-than-temporary based on this review.

The following table presents the cumulative credit related losses recognized in earnings on debt securities held by the Company as of:

(in millions)	December 31, 2013	December 31, 2012	December 31, 2011
Cumulative balance through January 1	$55	$38	$24
Credit impairments recognized in earnings on securities not previously impaired	—	1	1
Credit impairments recognized in earnings on securities that have been previously impaired	8	23	18
Reductions due to increases in cash flow expectations on impaired securities	(7)	(7)	(5)
Cumulative balance through December 31	$56	$55	$38

Cumulative credit losses recognized in earnings for impaired AFS debt securities held as of December 31, 2013, 2012, and 2011 were $56 million, $55 million, and $38 million, respectively. There were no credit losses recognized in earnings for the Company's HTM portfolio as of December 31, 2013 and 2012. The Company recognized $8 million, $24 million, and $19 million of credit related other-than-temporary impairment losses in earnings for the years ended December 31, 2013, 2012, and 2011, respectively, related to non-agency MBS in the AFS portfolio. No impaired debt securities were sold during 2013, 2012, or 2011. Reductions in credit losses due to increases in cash flow expectations were $7 million for the years ended December 31, 2013 and 2012, and $5 million for the year ended December 31, 2011, and are presented in investment securities interest income on the Consolidated Statements of Operations. The Company does not currently have the intent to sell these securities, and it is not likely that the Company will be required to sell these securities prior to the recovery of their amortized cost bases. As of December 31, 2013, 2012, and 2011, $41 million, $60 million, and $170 million, respectively, of pre-tax non-credit related losses were deferred in OCI.

The Company has determined that credit losses are not expected to be incurred on the remaining agency and non-agency MBS identified with unrealized losses as of the current reporting date. The unrealized losses on these investment securities reflect the reduced liquidity in the MBS market and the increased risk spreads due to the uncertainty of the U. S. macroeconomic environment. Therefore, the Company has determined that these securities are not other-than-temporarily impaired because the Company does not currently have the intent to sell these securities, and it is not likely that the Company will be required to sell these securities prior to the recovery of their amortized cost bases. Additionally, any subsequent increases in the valuation of impaired securities do not impact their recorded cost bases.

The amortized cost and fair value of debt securities at December 31, 2013 by contractual maturity are shown below. Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties.

	Distribution of Maturities				
(in millions)	1 Year or Less	1-5 Years	5-10 Years	After 10 Years	Total
Amortized Cost:					
Available for sale debt securities					
U.S. Treasury	$15	$0	$0	$0	$15
State and political subdivisions	—	—	—	11	11
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	—	39	2,865	12,066	14,970
Other / non-agency	—	43	120	829	992
Total available for sale debt securities	$15	$82	$2,985	$12,906	$15,988
Held to maturity debt securities					
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	$0	$0	$0	$2,940	$2,940
Other / non-agency	—	—	—	1,375	1,375
Total held to maturity debt securities	—	—	—	4,315	4,315
Total debt securities	$15	$82	$2,985	$17,221	$20,303
Fair Value:					
Available for sale debt securities					
U.S. Treasury	$15	$0	$0	$0	$15
State and political subdivisions	—	—	—	10	10
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	—	41	2,853	12,099	14,993
Other / non-agency	—	43	123	786	952
Total available for sale debt securities	$15	$84	$2,976	$12,895	$15,970
Held to maturity debt securities					
Mortgage-backed securities:					
Federal agencies and U.S. government sponsored entities	$0	$0	$0	$2,907	$2,907
Other / non-agency	—	—	—	1,350	1,350
Total held to maturity debt securities	—	—	—	4,257	4,257
Total debt securities	$15	$84	$2,976	$17,152	$20,227

Realized gains and losses on AFS securities are shown below:

	Years Ended December 31,		
(in millions)	2013	2012	2011
Gains on sale of debt securities	$144	$93	$170
Losses on sale of debt securities	—	—	(9)
Gains on sale of marketable equity securities	—	2	1
Total	$144	$95	$162

The amortized cost and fair value of securities pledged are shown below:

	December 31, 2013		December 31, 2012	
(in millions)	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Pledged against repurchase agreements	$5,016	$4,998	$2,882	$2,988
Pledged against Federal Home Loan Bank borrowed funds	1	1	6	6
Pledged against derivatives, to qualify for fiduciary powers, and to secure public and other deposits as required by law	2,818	2,853	4,995	5,184

Securitizations of mortgage loans retained in the investment portfolio for the years ended December 31, 2013, 2012, and 2011 were $106 million, $21 million, and $62 million, respectively. These securitizations included a substantive guarantee by a third party. In 2013, the guarantors were Fannie Mae, Ginnie Mae, and Freddie Mac, which purchased the underlying loans. In 2012, the guarantors were Fannie Mae and Freddie Mac. Fannie Mae guaranteed the 2011 securitizations. These securitizations were accounted for as a sale of the transferred loans and as a purchase of securities. The securities received from the guarantors are classified as AFS.

The Company regularly enters into security repurchase agreements with unrelated counterparties. Repurchase agreements are financial transactions that involve the transfer of a security from one party to another and a subsequent transfer of the same (or 'substantially the same') security back to the original party. The Company's repurchase agreements are typically short term (e.g., overnight) transactions, but they may be extended to longer terms to maturity. Such transactions are accounted for as secured borrowed funds on the Company's financial statements. When permitted by U.S. GAAP, the Company offsets the short-term receivables associated with its reverse repurchase agreements with the short-term payables associated with its repurchase agreements.

The effects of this offsetting on the Consolidated Balance Sheets are presented in the following table:

	December 31, 2013			December 31, 2012		
(in millions)	Gross Assets (Liabilities)	Gross Assets (Liabilities) Offset	Net Amounts of Assets (Liabilities)	Gross Assets (Liabilities)	Gross Assets (Liabilities) Offset	Net Amounts of Assets (Liabilities)
Reverse repurchase and similar arrangements	$0	$0	$0	$5,100	($4,000)	$1,100
Repurchase and similar arrangements	(3,000)	—	(3,000)	(4,000)	4,000	—

Note: The Company also offsets certain derivative assets and derivative liabilities on the Consolidated Balance Sheets. See Derivatives for further information.

NOTE 4 - LOANS AND LEASES

A summary of the loans and leases portfolio follows:

(in millions)	December 31, 2013	December 31, 2012
Commercial	$28,667	$28,856
Commercial real estate	6,948	6,459
Leases	3,780	3,415
Total commercial	39,395	38,730
Residential	29,694	31,101
Home equity products serviced by others	2,171	2,960
Other secured retail	10,700	10,568
Unsecured retail	3,899	3,889
Total retail	46,464	48,518
Total loans and leases	$85,859	$87,248

Excluded from the table above are loans totaling $1.1 billion, which were reclassified to loans held for sale at December 31, 2013. See Note 17 "Divestitures and Branch Assets and Liabilities Held for Sale" for further discussion.

Mortgage loans serviced for others by the Company's subsidiaries are not included above, and amounted to $18.7 billion and $18.6 billion at December 31, 2013 and 2012, respectively.

Loans pledged as collateral for FHLB borrowed funds totaled $19.0 billion and $22.9 billion at December 31, 2013 and 2012, respectively. This collateral consists primarily of residential mortgages and home equity loans. Loans pledged as collateral to support the contingent ability to borrow at the FRB discount window, if necessary, totaled $13.9 billion and $17.7 billion at December 31, 2013 and 2012, respectively.

In 2012, the Company purchased a portfolio of auto loans with outstanding principal balances of $922 million. It also sold a portfolio of commercial real estate loans totaling $227 million incurring a loss on sale of $23 million that is presented in other net gains in the accompanying Consolidated Statements of Operations.

The Company is engaged in the leasing of equipment for commercial use, with primary lease concentrations to Fortune 1000 companies for large capital equipment acquisitions. A lessee is evaluated from a credit perspective using the same underwriting standards and procedures as for a loan borrower. A lessee is expected to make rental payments based on its cash flows and the viability of its balance sheet. Leases are usually not evaluated as collateral-based transactions, and therefore the lessee’s overall financial strength is the most important credit evaluation factor.

A summary of the investment in leases, before the allowance for lease losses, is as follows:

(in millions)	**December 31, 2013**	**December 31, 2012**
Direct financing leases	$3,668	$3,260
Leveraged leases	112	155
Total leases	$3,780	$3,415

The components of the investment in leases before the allowance for lease losses are as follows:

(in millions)	**December 31, 2013**	**December 31, 2012**
Total future minimum lease rentals	$3,252	$3,186
Estimated residual value of leased equipment (unguaranteed)	968	678
Initial direct costs	20	13
Unearned income on minimum lease rentals and estimated residual value of leased equipment	(460)	(462)
Total leases	$3,780	$3,415

At December 31, 2013, the future minimum lease rentals on direct financing and leveraged leases are as follows:

Years Ended December 31,	(in millions)
2014	$675
2015	614
2016	501
2017	388
2018	363
Thereafter	711
Total	$3,252

Pre-tax income on leveraged leases was $3 million for the years ended December 31, 2013 and 2012 and $6 million for the year ended December 31, 2011. The income tax expense on this income was $1 million for the years ended December 31, 2013 and 2012 and $2 million for the year ended December 31, 2011. There was no investment credit recognized in income during these years.

NOTE 5 - ALLOWANCE FOR CREDIT LOSSES, NONPERFORMING ASSETS, AND CONCENTRATIONS OF CREDIT RISK

The ALLL is increased through a provision for credit losses that is charged to earnings, based on the Company's quarterly evaluation, and is reduced by net charge-offs and the ALLL associated with sold loans. See Note 1, Significant Accounting Policies, for a detailed discussion of ALLL methodologies and estimation techniques.

During 2013, the Company modified the way that it establishes the ALLL. As discussed in Note 1, the ALLL is reviewed separately for commercial and retail segments, and the ALLL for each includes an adjustment for qualitative reserves that includes certain risks, factors and events that might not be measured in the statistical analysis. As a result of this change, the unallocated reserve was absorbed into the separately measured commercial and retail qualitative reserves.

Additionally, during December 2013, the Company revised and extended its incurred loss period for certain residential mortgages. This change reflects management's recognition that incurred but unrealized losses emerge differently during various points of an economic / business cycle. ILPs are not static and move over time based on several factors. As economies expand and contract, access to credit, jobs, and liquidity moves directionally with the economy. Conceptually, the concept is very intuitive: ILPs will be longer in stronger economic times, when borrowers have the financial ability to withstand adversity and the ILPs will be shorter in an adverse economic environment, when the borrower has less financial flexibility. Since the current economy has not been as strong as 2002 – 2006 time period, we believe that ILPs will not be as long, but rather directional to our history. Since overall Company reserves are deemed adequate, there was no need to increase the reserve but rather reallocate some of the general reserves to cover the $96 million incurred loss period increase.

There were no other material changes in assumptions or estimation techniques compared with prior periods that impacted the determination of the current period's ALLL and the reserve for unfunded lending commitments.

The following is a summary of changes in the allowance for credit losses:

	Year Ended December 31, 2013			
(in millions)	Commercial	Retail	Unallocated	Total
Allowance for loan and lease losses as of January 1, 2013	$509	$657	$89	$1,255
Charge-offs	(108)	(595)	—	(703)
Recoveries	87	115	—	202
Net charge-offs	(21)	(480)	—	(501)
Sales / Other	(6)	(6)	(1)	(13)
Provision charged to income	(19)	396	103	480
Transfer of unallocated reserve to qualitative reserve	35	60	(95)	—
Loss emergence period change	—	96	(96)	—
Allowance for loan and lease losses as of December 31, 2013	498	723	—	1,221
Reserve for unfunded lending commitments as of January 1, 2013	40	—	—	40
Credit for unfunded lending commitments	(1)	—	—	(1)
Reserve for unfunded lending commitments as of December 31, 2013	39	—	—	39
Total allowance for credit losses as of December 31, 2013	$537	$723	$0	$1,260

	Year Ended December 31, 2012			
(in millions)	Commercial	Retail	Unallocated	Total
Allowance for loan and lease losses as of January 1, 2012	$691	$816	$191	$1,698
Charge-offs	(257)	(853)	—	(1,110)
Recoveries	113	122	—	235
Net charge-offs	(144)	(731)	—	(875)
Sales / Other	(2)	—	—	(2)
Provision charged to income	(36)	572	(102)	434
Allowance for loan and lease losses as of December 31, 2012	509	657	89	1,255
Reserve for unfunded lending commitments as of January 1, 2012	61	—	—	61
Credit for unfunded lending commitments	(21)	—	—	(21)
Reserve for unfunded lending commitments as of December 31, 2012	40	—	—	40
Total allowance for credit losses as of December 31, 2012	$549	$657	$89	$1,295

	Year Ended December 31, 2011			
(in millions)	Commercial	Retail	Unallocated	Total
Allowance for loan and lease losses as of January 1, 2011	$828	$1,021	$156	$2,005
Charge-offs	(378)	(1,008)	—	(1,386)
Recoveries	92	129	—	221
Net charge-offs	(286)	(879)	—	(1,165)
Sales/other	—	—	(33)	(33)
Provision charged to income	149	674	68	891
Allowance for loan and lease losses as of December 31, 2011	691	816	191	1,698
Reserve for unfunded lending commitments as of January 1, 2011	70	—	—	70
Credit for unfunded lending commitments	(9)	—	—	(9)
Reserve for unfunded lending commitments as of December 31, 2011	61	—	—	61
Total allowance for credit losses as of December 31, 2011	$752	$816	$191	$1,759

The recorded investment in loans and leases based on the Company's evaluation methodology is as follows:

	December 31, 2013			December 31, 2012		
(in millions)	Commercial	Retail	Total	Commercial	Retail	Total
Individually evaluated	$239	$1,200	$1,439	$474	$1,140	$1,614
Formula-based evaluation	39,156	45,264	84,420	38,256	47,378	85,634
Total	$39,395	$46,464	$85,859	$38,730	$48,518	$87,248

The following is a summary of the allowance for credit losses by evaluation method:

	December 31, 2013				December 31, 2012			
(in millions)	Commercial	Retail	Unallocated	Total	Commercial	Retail	Unallocated	Total
Individually evaluated	$23	$108	$0	$131	$41	$73	$0	$114
Formula-based evaluation	514	615	—	1,129	508	584	—	1,092
Unallocated	—	—	—	—	—	—	89	89
Allowance for credit losses	$537	$723	$0	$1,260	$549	$657	$89	$1,295

For commercial loans and leases, the Company utilizes regulatory classification ratings to monitor credit quality. Loans with a "pass" rating are those that the Company believes will be fully repaid in accordance with the contractual loan terms. Commercial loans and leases that are "criticized" are those that have some weakness that indicates an increased probability of future loss. For retail loans, the Company primarily uses the loan's payment and delinquency status to monitor credit quality. The further a loan is past due, the greater the likelihood of future credit loss. These credit quality indicators for both commercial and retail loans are continually updated and monitored.

The recorded investment in classes of commercial loans and leases based on regulatory classification ratings is as follows:

	December 31, 2013				
		Criticized			
(in millions)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$27,433	$588	$541	$105	$28,667
Commercial real estate	6,366	339	116	127	6,948
Leases	3,679	40	61	—	3,780
Total	$37,478	$967	$718	$232	$39,395

	December 31, 2012				
		Criticized			
(in millions)	Pass	Special Mention	Substandard	Doubtful	Total
Commercial	$27,100	$744	$809	$203	$28,856
Commercial real estate	5,285	569	315	290	6,459
Leases	3,304	88	23	—	3,415
Total	$35,689	$1,401	$1,147	$493	$38,730

The recorded investment in classes of retail loans, categorized by delinquency status is as follows:

	December 31, 2013				
(in millions)	Current	1-29 Days Past Due	30-89 Days Past Due	90 Days or more Past Due	Total
Residential	$27,912	$861	$259	$662	$29,694
Home equity products serviced by others	1,901	167	43	60	2,171
Other secured retail	10,068	550	66	16	10,700
Unsecured retail	3,593	185	67	54	3,899
Total	$43,474	$1,763	$435	$792	$46,464

	December 31, 2012				
(in millions)	Current	1-29 Days Past Due	30-89 Days Past Due	90 Days or more Past Due	Total
Residential	$29,075	$967	$230	$829	$31,101
Home equity products serviced by others	2,595	188	62	115	2,960
Other secured retail	9,938	545	74	11	10,568
Unsecured retail	3,633	123	78	55	3,889
Total	$45,241	$1,823	$444	$1,010	$48,518

The presentation of student loans at December 31, 2012 in the table above, and in the tables that follow, were reclassified from the other secured retail loan class to the unsecured retail loan class to conform to the Company's current loan class presentation.

Nonperforming Assets

A summary of nonperforming loans and leases by class follows:

	December 31, 2013			December 31, 2012		
(in millions)	Nonaccruing	Accruing and 90 Days or More Delinquent	Total Nonperforming Loans and Leases	Nonaccruing	Accruing and 90 Days or More Delinquent	Total Nonperforming Loans and Leases
Commercial	$96	$0	$96	$119	$71	$190
Commercial real estate	169	—	169	386	33	419
Leases	—	—	—	1	—	1
Total commercial	265	—	265	506	104	610
Residential	981	—	981	1,043	—	1,043
Home equity products serviced by others	89	—	89	133	—	133
Other secured retail	26	—	26	25	—	25
Unsecured retail	22	33	55	23	35	58
Total retail	1,118	33	1,151	1,224	35	1,259
Total	$1,383	$33	$1,416	$1,730	$139	$1,869

A summary of other nonperforming assets is as follows:

(in millions)	December 31, 2013	December 31, 2012
Nonperforming assets, net of allowance:		
Commercial	$10	$36
Retail	40	58
Nonperforming assets, net of allowance	$50	$94

Nonperforming assets consists primarily of other real estate owned and is presented in other assets on the Consolidated Balance Sheets.

A summary of key performance indicators is as follows:

	December 31, 2013	December 31, 2012
Nonperforming commercial loans and leases as a percentage of total loans and leases	0.31%	0.70%
Nonperforming retail loans as a percentage of total loans and leases	1.34	1.44
Total nonperforming loans and leases as a percentage of total loans and leases	1.65	2.14
Nonperforming commercial assets as a percentage of total assets	0.23	0.51
Nonperforming retail assets as a percentage of total assets	0.97	1.04
Total nonperforming assets as a percentage of total assets	1.20%	1.55%

The following is an analysis of the age of the past due amounts (accruing and nonaccruing):

	December 31, 2013			December 31, 2012		
(in millions)	30-89 Days Past Due	90 Days or more Past Due	Total Past Due	30-89 Days Past Due	90 Days or more Past Due	Total Past Due
Commercial	$61	$96	$157	$48	$190	$238
Commercial real estate	34	169	203	47	419	466
Leases	24	—	24	7	1	8
Total commercial	119	265	384	102	610	712
Residential	259	662	921	230	829	1,059
Home equity products serviced by others	43	60	103	62	115	177
Other secured retail	66	16	82	74	11	85
Unsecured retail	67	54	121	78	55	133
Total retail	435	792	1,227	444	1,010	1,454
Total	$554	$1,057	$1,611	$546	$1,620	$2,166

Impaired loans include (1) nonaccruing larger balance commercial loans (greater than $3 million carrying value) and (2) commercial and retail TDRs. The following is a summary of impaired loan information by class:

	December 31, 2013						
(in millions)	Impaired Loans With a Related Allowance	Allowance on Impaired Loans	Impaired Loans Without a Related Allowance	Unpaid Contractual Balance	Total Recorded Investment in Impaired Loans	Interest Income Recognized	Average Recorded Investment
Commercial	$86	$15	$33	$214	$119	$1	$157
Commercial real estate	76	8	44	221	120	1	149
Total commercial	162	23	77	435	239	2	306
Residential	355	59	497	1,081	852	14	737
Home equity products serviced by others	91	11	21	125	112	5	114
Other secured retail	23	3	12	43	35	1	33
Unsecured retail	201	35	—	201	201	10	181
Total retail	670	108	530	1,450	1,200	30	1,065
Total as of December 31, 2013	$832	$131	$607	$1,885	$1,439	$32	$1,371

	December 31, 2012						
(in millions)	Impaired Loans With a Related Allowance	Allowance on Impaired Loans	Impaired Loans Without a Related Allowance	Unpaid Contractual Balance	Total Recorded Investment in Impaired Loans	Interest Income Recognized	Average Recorded Investment
Commercial	$138	$25	$50	$321	$188	$1	$276
Commercial real estate	133	16	153	448	286	1	310
Total commercial	271	41	203	769	474	2	586
Residential	268	41	536	1,003	804	6	474
Home equity products serviced by others	122	16	33	194	155	6	127
Other secured retail	28	5	15	49	43	1	33
Unsecured retail	138	11	—	138	138	—	11
Total retail	556	73	584	1,384	1,140	13	645
Total as of December 31, 2012	$827	$114	$787	$2,153	$1,614	$15	$1,231

Troubled Debt Restructurings

A loan modification is identified as a TDR when the Company or a bankruptcy court grants the borrower a concession the Company would not otherwise make in response to the borrower's financial difficulties. Concessions granted in TDRs for all classes of loans may include lowering the interest rate, forgiving a portion of principal, extending the loan term, lowering scheduled payments for a specified period of time, principal forbearance, or capitalizing past due amounts. A rate increase can be a concession if the increased rate is lower than a market rate for debt with risk similar to that of the restructured loan. TDRs for commercial loans and leases may also involve creating a multiple note structure, accepting non-cash assets, accepting an equity interest, or receiving a performance-based fee. In some cases a TDR may involve multiple concessions. The financial effects of TDRs for all loan classes may include lower income (either due to a lower interest rate or a delay in the timing of cash flows), larger loan loss provisions, and accelerated charge-offs if the modification renders the loan collateral-dependent. In some cases interest income throughout the term of the loan may increase if, for example, the loan is extended or the interest rate is increased as a result of the restructuring.

Because TDRs are impaired loans, the Company measures impairment by comparing the present value of expected future cash flows, or, when appropriate, collateral value, to the loan's recorded investment. Any excess of recorded investment over the present value of expected future cash flows or collateral value is recognized by creating a valuation allowance or increasing an existing valuation allowance. Any portion of the loan's recorded investment the Company does not expect to collect as a result of the modification is charged off at the time of modification.

Commercial TDRs were $167 million and $244 million on December 31, 2013 and 2012, respectively. Retail TDRs totaled $1.2 billion and $1.1 billion on December 31, 2013 and 2012, respectively. Commitments to lend additional funds to debtors owing receivables which were TDRs were $52 million and $86 million on December 31, 2013 and 2012, respectively.

The following table summarizes how loans were modified during the year ending December 31, 2013, the charge-offs related to the modifications, and the impact on the ALLL. The reported balances include loans that became TDRs during 2013, and were paid off in full, charged off, or sold prior to December 31, 2013.

	Primary Modification Types					
	Interest Rate Reduction[1]			Maturity Extension[2]		
(dollars in millions)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial	126	$13	$13	134	$18	$18
Commercial real estate	11	7	7	3	1	1
Total commercial	137	20	20	137	19	19
Residential	414	48	50	2,221	91	82
Home equity products serviced by others	34	2	2	6	—	—
Other secured retail	259	2	2	2	—	—
Unsecured retail	2,729	15	15	—	—	—
Total retail	3,436	67	69	2,229	91	82
Total	3,573	$87	$89	2,366	$110	$101

	Primary Modification Types				
	Other[3]				
(dollars in millions)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Net Change to ALLL Resulting from Modification	Charge-offs Resulting from Modification
Commercial	6	$1	$1	$0	$1
Commercial real estate	1	—	—	(2)	—
Total commercial	7	1	1	(2)	1
Residential	2,196	174	160	4	23
Home equity products serviced by others	312	14	11	(1)	4
Other secured retail	1,471	16	13	—	4
Unsecured retail	2,620	48	47	5	—
Total retail	6,599	252	231	8	31
Total	6,606	$253	$232	$6	$32

(1) Includes modifications that consist of multiple concessions, one of which is an interest rate reduction.

(2) Includes modifications that consist of multiple concessions, one of which is a maturity extension (unless one of the other concessions was an interest rate reduction).

(3) Includes modifications other than interest rate reductions or maturity extensions, such as lowering scheduled payments for a specified period of time, principal forbearance, capitalizing arrearages, and principal forgiveness. Also included are the following: deferrals, trial modifications, certain bankruptcies, loans in forbearance and prepayment plans. Modifications can include the deferral of accrued interest resulting in post modification balances being higher than pre-modification.

The following table summarizes how loans were modified during the year ending December 31, 2012, the charge-offs related to the modifications, and the impact on the ALLL. The reported balances include loans that became TDRs during 2012, and were paid off in full, charged off, or sold prior to December 31, 2012.

	Primary Modification Types					
	Interest Rate Reduction(1)			Maturity Extension(2)		
(dollars in millions)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment
Commercial	18	$13	$13	108	$25	$24
Commercial real estate	4	9	9	6	14	13
Total commercial	22	22	22	114	39	37
Residential	565	95	99	193	14	16
Home equity products serviced by others	44	2	2	7	1	—
Unsecured retail	2,965	17	16	—	—	—
Total retail	3,574	114	117	200	15	16
Total	3,596	$136	$139	314	$54	$53

	Primary Modification Types				
	Other(3)				
(dollars in millions)	Number of Contracts	Pre-Modification Outstanding Recorded Investment	Post-Modification Outstanding Recorded Investment	Net Change to ALLL Resulting from Modification	Charge-offs Resulting from Modification
Commercial	180	$43	$46	($29)	$14
Commercial real estate	16	72	74	(26)	2
Total commercial	196	115	120	(55)	16
Residential	6,221	425	384	(6)	43
Home equity products serviced by others	1,514	67	50	(8)	17
Other secured retail	3,201	25	17	(4)	8
Unsecured retail	7,557	139	138	5	—
Total retail	18,493	656	589	(13)	68
Total	18,689	$771	$709	($68)	$84

(1) Includes modifications that consist of multiple concessions, one of which is an interest rate reduction.

(2) Includes modifications that consist of multiple concessions, one of which is a maturity extension (unless one of the other concessions was an interest rate reduction).

(3) Includes modifications other than interest rate reductions or maturity extensions, such as lowering scheduled payments for a specified period of time, principal forbearance, capitalizing arrearages, and principal forgiveness. Also included are the following: deferrals, trial modifications, certain bankruptcies, loans in forbearance and prepayment plans. Modifications can include the deferral of accrued interest resulting in post modification balances being higher than pre-modification.

The table below summarizes TDRs that defaulted during 2013 and 2012 within 12 months of their modification date. For purposes of this table, a payment default is defined as being past due 90 days or more under the modified terms. Amounts represent the loan's recorded investment at the time of payment default. Loan data in this table includes loans meeting the criteria that were paid off in full, charged off, or sold prior to December 31, 2013 and 2012. If a TDR of any loan type becomes 90 days past due after being modified the loan is written down to fair value less cost to sell. The amount written off is charged to the ALLL.

	2013		2012	
(dollars in millions)	Number of Contracts	Balance Defaulted	Number of Contracts	Balance Defaulted
Commercial	18	$1	4	$3
Commercial real estate	3	1	1	5
Total commercial	21	2	5	8
Residential	1,660	124	713	81
Home equity products serviced by others	229	5	208	15
Other secured retail	241	2	151	1
Unsecured retail	1,433	20	628	4
Total retail	3,563	151	1,700	101
Total	3,584	$153	1,705	$109

Concentrations of Credit Risk

Most of the Company's business activity is with customers located in the New England, Mid-Atlantic and Mid-West regions. Generally, loans are collateralized by assets including real estate, inventory, accounts receivable, other personal property and investment securities. As of December 31, 2013 and 2012, the Company had a significant amount of loans collateralized by residential and commercial real estate. There are no significant concentrations to particular industries within the commercial loan portfolio. Exposure to credit losses arising from lending transactions may fluctuate with fair values of collateral supporting loans, which fail to perform according to contractual agreements. The Company's policy is to collateralize loans to the extent necessary; however, unsecured loans are also granted on the basis of the financial strength of the applicant and the facts surrounding the transaction.

Certain loan products, including residential mortgages, home equity loans and lines of credit, and credit cards, have contractual features that may increase credit exposure to the Company in the event of an increase in interest rates or a decline in housing values. These products include loans that exceed 90% of the value of the underlying collateral (high LTV loans), interest-only and negative amortization residential mortgages, and loans with low introductory rates. Certain loans have more than one of these characteristics.

The following table presents balances of loans with these characteristics:

	December 31, 2013					December 31, 2012				
(in millions)	Residential Mortgages	Home Equity Loans & Lines of Credit	Home Equity Products Serviced by Others	Credit Cards	Total	Residential Mortgages	Home Equity Loans & Lines of Credit	Home Equity Products Serviced by Others	Credit Cards	Total
High loan-to-value	$1,054	$2,798	$1,581	$0	$5,433	$1,892	$4,685	$2,266	$0	$8,843
Interest only / negative amortization	882	—	—	—	882	868	—	—	—	868
Low introductory rate	—	—	—	119	119	—	—	—	118	118
Multiple characteristics & other	96	—	—	—	96	233	—	—	—	233
Total	$2,032	$2,798	$1,581	$119	$6,530	$2,993	$4,685	$2,266	$118	$10,062

NOTE 6 - PREMISES, EQUIPMENT, AND SOFTWARE

A summary of the carrying value of premises and equipment follows:

(dollars in millions)	Useful Lives	December 31, 2013	December 31, 2012
Land and land improvements	15 years	$33	$48
Buildings and leasehold improvements	5-40 years	636	669
Furniture, fixtures and equipment	5-10 years	1,598	1,671
Total premises and equipment, gross		2,267	2,388
Less: accumulated depreciation		1,675	1,745
Total premises and equipment, net		$592	$643

The above table includes capital leases with book values of $45 million and $53 million and related accumulated depreciation of $17 million and $37 million as of December 31, 2013 and 2012, respectively. Depreciation charged to noninterest expense was $138 million, $163 million, and $179 million for the years ended December 31, 2013, 2012, and 2011, respectively, and is presented in the Consolidated Statements of Operations in occupancy and equipment expense.

The Company entered into a sale-leaseback transaction during 2013, which includes an operating lease for a period of 10 years. There was a $15 million gain recorded in 2013 of which $14 million was deferred. There were no sale-leaseback transactions during 2012. During 2011, The Company entered into a sale-leaseback transaction, which included an operating lease for a period of 10 years. There was a $1 million gain recorded in 2011 and the entire amount was deferred. The deferred gains on the Company’s sale-leaseback transactions are amortized over the lease terms and reported in occupancy expense.

The Company had capitalized software assets, net of amortization, of $729 million and $623 million as of December 31, 2013 and 2012 respectively. Amortization expense was $102 million, $77 million, and $53 million for the years ended December 31, 2013, 2012, and 2011, respectively. Capitalized software assets are reported as a component of Other assets in the Consolidated Balance Sheets.

The estimated future amortization expense for capitalized software assets is as follows:

Year	(in millions)
2014	$108
2015	92
2016	73
2017	56
2018	33
Thereafter	133
Total	$495

NOTE 7 - LEASE COMMITMENTS

The Company is committed under long-term leases for the rental of premises and equipment. These leases have varying renewal options and require, in certain instances, the payment of insurance, real estate taxes and other operating expenses.

At December 31, 2013, the aggregate minimum rental commitments under these non-cancelable operating leases and capital leases, exclusive of renewals, are as follows for the years ended December 31,:

(in millions)	Operating Leases	Capital Leases
2014	$173	$10
2015	161	7
2016	146	7
2017	119	6
2018	84	2
Thereafter	213	8
Total minimum lease payments	$896	$40
Amounts representing interest	n/a	(9)
Present value of net minimum lease payments	n/a	$31

Rental expense for such leases for the years ended December 31, 2013, 2012, and 2011 totaled $224 million, $203 million, and $228 million, respectively, and is presented in the Consolidated Statements of Operations in occupancy and equipment expense.

NOTE 8 - GOODWILL

Goodwill

The changes in the carrying value of goodwill for the years ended December 31, 2013, 2012, and 2011 were:

(in millions)	Retail	Commercial
Balance as of December 31, 2011	$6,393	$4,918
Impairment losses based on results of interim impairment testing	—	—
Balance as of December 31, 2012	$6,393	$4,918
Impairment losses based on results of interim impairment testing	(4,435)	—
Transfers	178	(178)
Balance as of December 31, 2013	$2,136	$4,740

Accumulated impairment losses related to the Retail Banking reporting unit totaled $5.9 billion at December 31, 2013, and $1.5 billion at December 31, 2012 and 2011. The accumulated impairment losses related to the Commercial Banking unit at December 31, 2013, 2012 and 2011 totaled $50 million.

The Company performs an annual test for impairment of goodwill at a level of reporting referred to as a reporting unit. The Company has identified and allocated goodwill to the following reporting units based upon reviews of the structure of the Company's executive team and supporting functions, resource allocations and financial reporting processes:

- Retail Banking
- Commercial Banking

During 2012, the Global Transaction Services reporting unit was combined with Commercial Banking following a reorganization of operations at RBSG.

The Company tested the value of goodwill as of June 30, 2013, and recorded an impairment charge of $4.4 billion in the Retail Banking reporting unit. The impairment charge, which was a non-cash item, had minimal impact on the Company's regulatory capital ratios and liquidity. No impairment was recorded in 2012 and 2011.

The valuation of goodwill is dependent on forward-looking expectations related to the performance of the U.S. economy and the associated financial performance of the Company. The prolonged delay in the full recovery of the U.S. economy, and the impact of that delay on earnings expectations, prompted a goodwill impairment test as of June 30, 2013. Although the U.S. economy has demonstrated signs of recovery, notably improvements in unemployment and housing, the pace and extent of recovery in these indicators, as well as in overall Gross Domestic Product, have lagged previous expectations. The impact of the slow recovery is most evident in the Company's Retail Banking reporting unit. Forecasted economic growth for the U.S., coupled with the continuing impact of the new regulatory framework in the financial industry, have resulted in a deceleration of expected growth for the Retail Banking reporting unit's future profits, and an associated goodwill impairment. Refer to Note 1 for information regarding the impairment test.

NOTE 9 - MORTGAGE BANKING

In its mortgage banking business, the Company sells residential mortgage loans to government-sponsored entities and other parties, who may issue securities backed by pools of such loans. The Company retains no beneficial interests in these sales, but may retain the servicing rights of the loans sold. The Company is obligated to subsequently repurchase a loan if the purchaser discovers a standard representation or warranty violation such as noncompliance with eligibility requirements, customer fraud, or servicing violations. This primarily occurs during a loan file review.

The Company received $4.2 billion, $5.4 billion, and $4.0 billion of proceeds from the sale of residential mortgages in 2013, 2012, and 2011, respectively and recognized gains on such sales of $66 million, $123 million, and $41 million in 2013, 2012, and 2011, respectively. Pursuant to the standard representations and warranties obligations discussed in the preceding paragraph, the Company repurchased mortgage loans totaling $35 million, $13 million, and $9 million in 2013, 2012, and 2011, respectively.

Mortgage servicing fees, a component of mortgage banking income, was $61 million for the year ended December 31, 2013 and $60 million for the years ended December 31, 2012 and 2011. The Company recorded a recovery of $47 million compared to impairments of $12 million and $42 million for its MSRs for the years ended December 31, 2013, 2012, and 2011, respectively.

Changes related to MSRs were as follows:

	Years Ended December 31,		
(in millions)	2013	2012	2011
MSRs:			
Balance as of January 1	$215	$215	$209
Amount capitalized	45	67	59
Amortization	(52)	(67)	(53)
Carrying amount before valuation allowance	208	215	215
Valuation allowance for servicing assets:			
Balance as of January 1	70	58	16
Valuation impairment (recovery)	(47)	12	42
Balance at end of period	23	70	58
Net carrying value of MSRs	$185	$145	$157

MSRs are presented in other assets on the Consolidated Balance Sheets.

The fair value of MSRs is estimated using a valuation model that calculates the present value of estimated future net servicing cash flows, taking into consideration actual and expected mortgage loan prepayment rates, discount rates, servicing costs, and other economic factors, which are determined based on current market conditions. The valuation model uses a static discounted cash flow methodology incorporating current market interest rates. A static model does not attempt to forecast or predict the future direction of interest rates; rather it estimates the amount and timing of future servicing cash flows using current market interest rates. The current mortgage interest rate influences the expected prepayment rate and therefore, the length of the cash flows associated with the servicing asset, while the discount rate determines the present value of those cash flows. Expected mortgage loan prepayment assumptions are obtained using the QRM Multi Component prepayment model. The Company periodically obtains third party valuations of its MSRs to assess the reasonableness of the fair value calculated by the valuation model.

The key economic assumptions used to estimate the value of mortgage MSRs are presented in the following tables:

(dollars in millions)	December 31, 2013	December 31, 2012
Fair value	$195	$147
Weighted average life (in years)	5.4	3.6
Weighted average constant prepayment rate	13.0%	21.4%
Weighted average discount rate	10.8%	10.5%

	Years Ended December 31,		
(in millions)	2013	2012	2011
Prepayment rate:			
Decline in fair value from 50 bps adverse change in interest rates	$9	$11	$18
Decline in fair value from 100 bps adverse change in interest rates	$18	$18	$25
Weighted average discount rate:			
Decline in fair value from 50 bps adverse change	$3	$2	$2
Decline in fair value from 100 bps adverse change	$6	$4	$4

The key economic assumptions used in estimating the fair value of MSRs capitalized during the year were as follows:

	Years Ended December 31,		
	2013	2012	2011
Weighted average life (in years)	6.0	4.0	5.0
Weighted average constant prepayment rate	12.4%	20.7%	16.2%
Weighted average discount rate	10.5%	10.5%	10.6%

A sensitivity analysis as of December 31, 2013 of current fair value to an immediate 50 bps and 100 bps adverse change in the key economic assumptions presents the decline in fair value that would occur if the adverse change were realized. These sensitivities are hypothetical. The effect of a variation in a particular assumption on the fair value of the mortgage servicing rights is calculated independently without changing any other assumption. In reality, changes in one factor may result in changes in another (for example, changes in interest rates, which drive changes in prepayment speeds, could result in changes in the discount rates), which might amplify or counteract the sensitivities. The primary risk inherent in the Company's MSRs is an increase in prepayments of the underlying mortgage loans serviced, which is dependent upon market movements of interest rates.

NOTE 10 - DEPOSITS

The major components of deposits are as follows:

(in millions)	December 31, 2013	December 31, 2012
Demand	$24,931	$25,931
Checking with interest	13,630	14,577
Regular savings	7,509	7,874
Money market accounts	31,245	35,102
Term deposits	9,588	11,664
Total deposits	$86,903	$95,148

The maturity distribution of term deposits as of December 31, 2013 is as follows:

Year	(in millions)
2014	$7,444
2015	985
2016	465
2017	431
2018 and thereafter	263
Total	$9,588

Of these deposits, the amount of term deposits with a denomination of $100,000 or more was $3.9 billion at December 31, 2013. The remaining maturities of these deposits are as follows:

	(in millions)
Three months or less	$2,221
After three months through six months	427
After six months through twelve months	718
After twelve months	570
Total term deposits	$3,936

Excluded from the tables above are deposits totaling $5.3 billion, which includes term deposits of $891 million, that were reclassified to deposits held for sale at December 31, 2013. See Note 17, "Divestitures and Branch Assets and Liabilities Held for Sale" for further discussion. Of these term deposits held for sale, term deposits with a denomination of $100,000 or more were $268 million as of December 31, 2013.

NOTE 11 - BORROWED FUNDS

The following is a summary of the Company's short-term borrowed funds:

	Years Ended December 31,	
(in millions)	**2013**	**2012**
Federal funds purchased	$689	$1,905
Securities sold under agreements to repurchase	4,102	1,696
Short-term borrowed funds	2,251	501
Total short-term borrowed funds	$7,042	$4,102

Key data related to short-term borrowed funds is presented in the following table:

	Years Ended December 31,		
(dollars in millions)	**2013**	**2012**	**2011**
Weighted average interest rate at year-end			
Federal funds purchased and securities sold under agreements to repurchase	0.09%	0.10%	0.06%
Short-term borrowed funds	0.20	0.29	0.20
Maximum amount outstanding at month-end during the year			
Federal funds purchased and securities sold under agreements to repurchase	$5,114	$4,393	$6,406
Short-term borrowed funds	2,251	5,050	4,000
Average amount outstanding during the year			
Federal funds purchased and securities sold under agreements to repurchase	$2,400	$2,716	$3,808
Short-term borrowed funds	259	3,045	2,645
Weighted average interest rate during the year			
Federal funds purchased and securities sold under agreements to repurchase	0.31%	0.22%	0.12%
Short-term borrowed funds	3.10	2.46	2.65

The following is a summary of the Company's long-term borrowed funds:

	As of December 31,	
(dollars in millions)	**2013**	**2012**
Parent company:		
4.150% subordinated debt, due 2022	$350	$350
5.158% subordinated debt, due 2023	333	—
4.771% subordinated debt, due 2023	333	—
4.691% subordinated debt, due 2024	334	—
1.860% subordinated debt, due 2035	—	289
Bank Subsidiaries:		
Federal Home Loan advances due through 2033	25	27
Other	30	28
Total long-term borrowed funds	$1,405	$694

Advances, lines of credit and letters of credit from the FHLB are collateralized by pledged mortgages and pledged securities at least sufficient to satisfy the collateral maintenance level established by the FHLB. The utilized borrowing capacity for FHLB advances and letters of credit was $4.2 billion and $1.1 billion at December 31, 2013 and 2012, respectively. The Company's available FHLB borrowing capacity was $8.2 billion and $12.8 billion at December 31, 2013 and 2012, respectively. The Company can also borrow from the FRB discount window to meet short-term liquidity requirements. These potential borrowed funds are secured by investment securities and loans. At December 31, 2013, the Company's unused secured borrowing capacity was approximately $28.9 billion, which includes free securities, FHLB borrowing capacity, and FRB discount window capacity. Additionally, at December 31, 2013, the Company had available a $50 million line of credit with RBSG.

The following is a summary of maturities for the Company's long-term borrowed funds at December 31, 2013:

Year	(in millions)
2014 or on demand	$0
2015	3
2016	6
2017	17
2018	13
2019 and thereafter	1,366
Total	$1,405

NOTE 12 - PREFERRED STOCK

The Company has authorized 30,000 shares of $1 par value non-cumulative, non-voting perpetual preferred stock as of December 31, 2013. The preferred stock ranks senior to the common stock of the Company with respect to dividend rights upon liquidation or dissolution of the Company. The stock is not convertible into any other property of the Company, nor is it redeemable by either the Company or the holder thereof. Dividends are non-cumulative and are payable quarterly at LIBOR plus 180 bps, if and when declared by the Company's board of directors. In the event of any liquidation, dissolution or winding up of the Company, holders of each share of the preferred stock outstanding are entitled to be paid, out of the assets of the Company available for distribution to stockholders, before any payment is made to the holders of common stock, an amount equal to $100,000 per share of preferred stock then issued and outstanding. There were no shares issued and outstanding during 2013 or 2012.

NOTE 13 - EMPLOYEE BENEFITS

Pension Plans

The Company maintains a non-contributory pension plan (the "Plan" or "qualified plan") that was closed to new-hires and re-hires effective January 1, 2009 and frozen to all participants effective December 31, 2012. Benefits under the Plan are based on employees' years of service and highest 5-year average eligible compensation. The Plan is funded on a current basis, in compliance with the requirements of the ERISA. The Company also provides an unfunded, non-qualified supplemental retirement plan (the "non-qualified plan") which was closed and frozen consistent with the qualified plan.

RBSG restructured the administration of employee benefit plans during 2008. As a result, the qualified and non-qualified pension plans of certain RBSG subsidiaries (referred to as the Company's "Affiliates") merged with the Company's pension plans. As plan sponsor of the surviving plans, the Company recorded the pension obligation or asset (for the entire qualified plan) and obligation (for the entire non-qualified plan) in the accompanying consolidated balance sheets as of December 31, 2013, 2012 and 2011.

During 2012, the Company offered to vested former employees who had not yet retired a one-time opportunity to receive the value of future defined benefit pension payments as a single lump sum payment. In December 2012, the Company made lump sum payments of $196 million to former employees who accepted the offer, which resulted in a $240 million reduction of the defined benefit obligation and a $92 million settlement charge.

The qualified plan's allocation by asset category is as follows:

	Target Asset Allocation 2014	Actual Asset Allocation	
		2013	2012
Asset Category			
Equity securities	45-55%	52.6%	54.2%
Debt securities	40-50%	42.9	40.2
Other	0-10%	4.5	5.6
Total		100.0%	100.0%

The written Pension Plan Investment Policy, set forth by the RBS Americas Retirement Committee, formulates those investment principles and guidelines that are appropriate to the needs and objectives of the Plan, and defines the management, structure, and monitoring procedures adopted for the ongoing operation of the aggregate funds of the Plan. Stated goals and objectives are:

- total return, consistent with prudent investment management, is the primary goal of the Plan. The nominal rate of return objective should meet or exceed the actuarial rate return target. In addition, assets of the Plan shall be invested to ensure that principal is preserved and enhanced over time;
- the total return for the overall Plan shall meet or exceed the Plan's Policy Index;
- total portfolio risk exposure should generally rank in the mid-range of comparable funds. Risk-adjusted returns are expected to consistently rank in the top-half of comparable funds; and
- investment managers shall exceed the return of the designated benchmark index and rank in the top-half of the appropriate asset class and style universe.

The RBS Americas Retirement Committee reviews, at least annually, the assets and net cash flow of the Plan, discusses the current economic outlook and the Plan's investment strategy with the investment managers, reviews the current asset mix and its compliance with the Policy, and receives and considers statistics on the investment performance of the Plan.

The Plan's investment advisors may vary equity commitments from 90% to 100% of assets under management. American Depository Receipts may be held by each domestic stock manager, in proportions that each manager shall deem appropriate. The maximum weight of the stock of any one company at the total portfolio level is 5% at market.

The minimum quality rating of any fixed income issue held in an investment grade portfolio should be B, and the overall weighted average quality should be A or higher. The overall quality of the high yield fixed income portfolio should be B or better. The average duration (interest rate sensitivity) of an actively managed fixed income portfolio should not exceed seven years.

Securities of an individual issuer, except the U.S. government and agencies and sovereign nations and their agencies, should not constitute more than 8% of an investment manager's portfolio at any time, at fair value.

The assets of the qualified plan may be invested in any or all of the following asset categories:

a) Equity-oriented investments:
   - domestic and foreign common and preferred stocks, and related rights, warrants, convertible debentures, and other common share equivalents
   - equity index futures, and options on equity index futures
   - exchange traded options on equities
   - venture capital funds / partnerships

b) Fixed income-oriented investments:
   - domestic and foreign bonds, debentures and notes
   - mortgages
   - mortgage-backed securities
   - asset-backed securities
   - guaranteed investment contracts or certificates
   - term deposits
   - money market securities or cash

- financial futures and options on financial futures
- forward contracts
- options on financial instruments

Unless specifically approved by the RBS Americas Retirement Committee, certain securities, strategies and investments are ineligible for inclusion within this Plan's asset base. Among these are:

- privately-placed or other non-marketable debt, except securities issued under Rule 144A;
- lettered, legend or other so-called restricted stock;
- commodities (only the PIMCO All Asset Fund has been approved, which invests in a variety of PIMCO funds, including the PIMCO Commodity Real Return Fund);
- straight preferred stocks and non-taxable municipal securities should not normally be held unless pricing anomalies in the marketplace suggest the likelihood of near-term capital gains when normal spread relationships resume;
- unhedged short sales (market neutral hedge fund has been approved);
- direct investments in private placements, real estate, oil and gas and venture capital; and
- any transaction prohibited by ERISA.

In addition, derivative instruments are permitted for the following reasons: hedging, creation of market exposures and management of country and asset allocation exposure. Derivative instruments are prohibited for the following reasons: leverage and unrelated speculation.

In selecting the expected long-term rate of return on assets, the Company considers the average rate of earnings expected on the funds invested or to be invested to provide for the benefits of this Plan. This includes considering the trust's asset allocation and the expected returns likely to be earned over the life of the Plan. This basis is consistent with the prior year.

Changes in the fair value of defined benefit pension plan assets, projected benefit obligation, funded status, and accumulated benefit obligation are summarized as follows:

	Years Ended December 31,					
	Qualified Plan			Non-Qualified Plan		
(in millions)	2013	2012	2011	2013	2012	2011
Fair value of plan assets as of January 1	$998	$1,106	$975	$0	$0	$0
Actual return (loss) on plan assets	111	142	(23)	—	—	—
Employer contributions	—	—	200	8	8	7
Settlements	—	(196)	—	—	—	—
Benefits and administrative expenses paid	(78)	(54)	(46)	(8)	(8)	(7)
Fair value of plan assets as of December 31	1,031	998	1,106	—	—	—
Projected benefit obligation	1,026	1,185	1,118	107	116	109
Pension asset (obligation)	$5	($187)	($12)	($107)	($116)	($109)
Accumulated benefit obligation	$1,026	$1,185	$1,100	$107	$116	$109

The table below summarizes the beneficial interest in the pension asset (obligation) for the qualified and non-qualified plans between the Company and Affiliates:

	Years Ended December 31,					
	Qualified Plan			Non-Qualified Plan		
(in millions)	2013	2012	2011	2013	2012	2011
RBS Citizens	$56	($116)	$33	($101)	($113)	($107)
Affiliates	(51)	(71)	(45)	(6)	(3)	(2)
Pension asset (obligation)	$5	($187)	($12)	($107)	($116)	($109)

The Company's share of the 2012 single lump sum payments to vested former employees described earlier in this Note for the qualified plan was $146 million, while $15 million of the lump sum payments were due from Affiliates as of December 31, 2012. There were no balances due to or due from Affiliates as of December 31, 2013 or December 31, 2011.

The pre-tax amounts recognized (for the qualified and non-qualified plans) in accumulated OCI as follows:

	December 31,	
(in millions)	**2013**	**2012**
Net prior service credit	$0	$0
Net actuarial loss	414	602
Total loss recognized in accumulated other comprehensive income	$414	$602

Approximately $10 million of net actuarial loss recorded in accumulated OCI as of December 31, 2013 is expected to be recognized as a component of net periodic benefit costs during 2014.

Other changes in plan assets and benefit obligations (for the qualified and non-qualified plans) recognized in OCI include the following:

	Years Ended December 31,		
(in millions)	**2013**	**2012**	**2011**
Net periodic pension (income) / cost	($3)	$150	$39
Net actuarial (gain) loss	(174)	169	242
Amortization of prior service credit	—	1	1
Amortization of net actuarial loss	(14)	(38)	(20)
Settlement	—	(92)	—
Total recognized in other comprehensive income	(188)	40	223
Total recognized in net periodic pension cost and other comprehensive income	($191)	$190	$262

There were no settlements for the years ended December 31, 2013 and 2011. The Company’s share of the $92 million settlement was $77 million for the year ended December 31, 2012.

Weighted average rates assumed in determining the actuarial present value of benefit obligations and net periodic benefit cost are as follows:

	Years Ended December 31,		
	2013	**2012**	**2011**
Assumptions for benefit obligations			
Discount rate--qualified plan	5.00%	4.125%	5.25%
Discount rate--non-qualified plan	4.75	4.00	5.00
Compensation increase rate	N/A	N/A	4.75
Expected long-term rate of return on plan assets	7.50	7.75	8.25
Assumptions for net periodic pension cost			
Discount rate--qualified plan	4.125	5.25	5.75
Discount rate--non-qualified plan	4.00	5.00	5.63
Compensation increases--qualified and non-qualified plans	N/A	4.75	4.75
Expected long-term rate of return on plan assets	7.50	7.75	8.25

The Company expects to contribute $8 million to its non-qualified plan in 2014.

The following benefit payments for the qualified and non-qualified plans reflect expected future service, as appropriate, that are expected to be paid:

(in millions)	
Expected benefit payments by fiscal year ended	
December 31, 2014	$65
December 31, 2015	65
December 31, 2016	66
December 31, 2017	67
December 31, 2018	68
December 31, 2019 - 2023	361

Fair Value Measurements

The following valuation techniques are used to measure the qualified pension plan assets at fair value:

Cash and money market funds:

Cash and money market funds represent instruments that generally mature in one year or less and are valued at cost which approximates fair value. Cash and money market funds are classified as Level 2.

Mutual funds:

Where observable quoted prices are available in an active market, mutual funds are classified as Level 1 in the fair value hierarchy. If quoted market prices are not available, mutual funds are classified as Level 2 because they currently trade in active markets and the Company expects all future purchases and sales to be valued at current net asset value.

Corporate bonds, municipal obligations, U.S. government obligations and Non-U.S. government obligations:

Corporate bonds, municipal obligations, U.S. government obligations and Non-U.S. government obligations are valued at the quoted market prices determined in the active markets in which the bonds are traded. If quoted market prices are not available, the fair value of the security is estimated using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. These investments are classified as Level 2, because they currently trade in active markets for similar securities and the inputs to the valuations are observable.

Limited partnerships:

Limited partnerships are valued at estimated fair value based on their proportionate share of the limited partnerships' fair value as recorded in the limited partnerships' audited financial statements. The limited partnerships invest primarily in readily marketable securities. The limited partnerships allocate gains, losses and expenses to the partners based on ownership percentage as described in the partnership agreements. The instruments that can be transacted at the investment net asset value are classified as Level 2 because the Company expects all future purchases and sales to be valued at current net asset value. The instruments that cannot be transacted at the investment net asset value are classified as Level 3 investments.

Common collective funds:

The fair value is estimated using the net asset value received from the investment companies. The instruments that can be transacted at the investment net asset value are classified as Level 2 because the Company expects all future purchases to be valued at current net asset value. Instruments that cannot be transacted at the investment net asset value are classified as Level 3 investments.

Derivatives-Managed portfolio:

The managed portfolio invests in certain derivatives which are valued at the settlement price determined by the relevant exchange and are classified as Level 2 in the fair value hierarchy.

The following tables present the qualified pension plan assets measured at fair value within the fair value hierarchy:

	Fair Value Measurements as of December 31, 2013			
(in millions)	Total	Level 1	Level 2	Level 3
Cash and money market funds	$8	$0	$8	$0
Mutual funds				
International equity funds	28	28	—	—
Income funds	43	—	43	—
Common and collective funds				
International equity common and collective funds	115	—	115	—
Balanced common and collective funds	474	—	474	—
Fixed income common and collective funds	117	—	117	—
Managed Fund				
Cash and money market funds	1	—	1	—
Corporate bonds	105	—	105	—
Municipal obligations	2	—	2	—
U.S. government obligations	9	—	9	—
Non-U.S. government obligations	3	—	3	—
Limited partnerships	126	—	126	—
Total assets measured at fair value	$1,031	$28	$1,003	$0

	Fair Value Measurements as of December 31, 2012			
	Total	Level 1	Level 2	Level 3
Cash and money market funds	$20	$0	$20	$0
Mutual funds				
International equity funds	31	31	—	—
Income funds	49	—	49	—
Common and collective funds				
International equity common and collective funds	115	—	115	—
Balanced common and collective funds	395	—	395	—
Fixed income common and collective funds	123	—	123	—
Managed Fund				
Cash and money market funds	5	—	5	—
U.S. government obligations	15	—	15	—
Municipal obligations	2	—	2	—
Corporate bonds	97	—	97	—
Non-U.S. government obligations	4	—	4	—
Derivative assets- swaps	1	—	1	—
Derivative liabilities- swaps	(1)	—	(1)	—
Limited partnerships	142	—	142	—
Total assets measured at fair value	$998	$31	$967	$0

In keeping with the Plan's fixed income strategic objectives, the December 31, 2013 holdings of the managed fund included exchange traded Eurodollar futures contracts with a notional value of $324 million and an unrealized gain (fair value) of under $1 million. There were no transfers among Levels 1, 2 or 3 during the years ended December 31, 2013, 2012, and 2011.

The fair values of participation units in the common and collective trusts are based on net asset value after adjustments to reflect all fund investments at fair value. The unfunded commitments, redemption frequency, and redemption notice period for those Plan investments that utilize net asset value to determine the fair value as of December 31, 2013 and 2012, are as follows:

Investments	**Fair Value Estimated Using Net Asset Value per Share as of December 31**					
(dollars in millions)	**2013**	**2012**	**Unfunded Commitment**	**Redemption Frequency**	**Redemption Restrictions**	**Notice Period**
Equity Mutual Fund[1]	$43	$49	—	Daily	None	1-7 days
Common and Collective Funds:						
Domestic equity funds[2]	0	0	—	Daily	None	5-15 days
International equity funds[3]	115	115	—	Monthly	None	3 days
Balanced funds[4]	474	395	—	Daily	None	2-3 days
Fixed income fund[5]	117	123	—	Daily	None	3 days
Limited Partnerships:						
International Equity[6]	116	130	—	Daily	None	10 days
Offshore Feeder Fund[7]	10	12	—	Monthly	None	14 days
Total	$875	$824				

[1] The equity mutual fund seeks to offer participants capital appreciation by primarily investing in common stocks via investments in several underlying funds of the same fund family. The principle investment objective is to generate positive total return.

[2] The domestic equity funds seek to offer participants capital appreciation by primarily investing in common stocks of companies domiciled in the U.S. Strategies may also include total return while limiting the exposure to the equity market risk.

[3] The international equity funds seek medium to long-term capital appreciation principally through global investments in readily marketable high-quality equity securities of companies with improving fundamentals and attractive valuations.

[4] The balanced funds seek to maximize total return by investing in global equities and fixed income transferable securities which may include some high yield fixed income transferable securities. The fund may invest in securities denominated in currencies other than U.S. dollars.

[5] The fixed income fund seeks to outperform the Barclays Capital U.S. Corporate Investment Grade Bond Index or similar benchmark.

[6] The international equity limited partnership focuses on global and agribusiness strategies, blending a thematic framework with security-level analysis and customized valuation techniques. The fund conducts primary research to identify investable themes that provide clients with diversification benefits and help create opportunities for outperformance over a market cycle.

[7] The offshore feeder fund operates under a "master / feeder" structure whereby it invests substantially all assets in the GMO Multi-Strategy Fund (Onshore) (the "master fund"). The investment objective of the master fund is capital appreciation with a target performance of the Citigroup Three-Month Treasury Bill plus 8% with a standard deviation of 5%. The investment advisor plans to pursue the master fund's objective through a combination of investments in other pooled vehicles.

Postretirement Benefits

The Company and Affiliates provide health care insurance benefits for certain retired employees and their spouses. Employees enrolled in medical coverage immediately prior to retirement and meeting eligibility requirements can elect retiree medical coverage. Employees and covered spouses can continue coverage at the full cost, except for a small group described below. However, coverage must be elected at the time of retirement and cannot be elected at a future date. Spouses may be covered only if the spouse is covered at the time of the employee's retirement.

The Company reviews coverage on an annual basis and reserves the right to modify or cancel coverage at any renewal date. The Company's cost sharing for certain full-time employees, who were hired prior to August 1, 1993 with 25 years of service who reach retirement age (under age 65) while employed by the Company is 70%; for those with 15-24 years of service, the Company's share is 50%. Also, the Company shares in the cost for retiree medical benefits for a closed group of grandfathered arrangements from acquisitions. A small, closed group of retirees receive life insurance coverage.

The accumulated postretirement benefit obligation was $27 million and $30 million at December 31, 2013 and 2012, respectively. The funded status was a liability of $27 million and $30 million at December 31, 2013 and 2012, respectively, and is reported in other liabilities in the accompanying consolidated balance sheets. The total gain recognized in OCI was $367 thousand at December 31, 2013 and a total cost recognized in OCI was $1 million at December 31, 2012.

The Company contributed and paid benefits of $3 million, $2 million, and $3 million during 2013, 2012 and 2011, respectively. The benefits expected to be paid in each of the next five years is $2 million, and $9 million is expected to be paid during the five years from 2019 through 2023. The Company expects to contribute approximately $2 million to the plan during 2014.

The weighted average discount rate assumed in determining the actuarial present value of benefit obligations was 4.625% and 3.88% as of December 31, 2013 and 2012, respectively.

For measurement purposes, a 7.5% and 8.0% assumed annual rate of increase in the per capita cost of covered health care benefits were used for the years ended December 31, 2013 and 2012, respectively, decreasing gradually down to a 5% ultimate rate over the next several years.

Postemployment Benefits

The Company provides postemployment benefits to certain former and inactive employees, primarily the Company's long-term disability plan. Effective January 1, 2013, the Company required claimants receiving long-term disability benefits for 24 months to apply for Medicare approval so that Medicare is the primary payer of medical benefits. (Benefit) Cost recorded for the years ended December 31, 2013, 2012 and 2011 were ($3) million, ($1) million, and $3 million, respectively.

401(k) Plan

The Company sponsors an employee tax-deferred 401(k) plan under which individual employee contributions to the plan are matched by the Company. For periods prior to 2012, contributions are matched at 100% up to an overall limitation of 6% on a pay period basis. Employees hired or rehired on or after January 1, 2009 receive an additional 3% of earnings, subject to limits set by the Internal Revenue Service. Effective January 1, 2013, contributions are matched at 100% up to an overall limitation of 5% on a pay period basis. Substantially all employees will receive an additional 2% of earnings, subject to limits set by the Internal Revenue Service. Amounts contributed by the Company for the years ended December 31, 2013, 2012, and 2011 were $70 million, $60 million, and $57 million, respectively.

NOTE 14 - INCOME TAXES

Total income tax (benefit) expense was as follows:

	Years Ended December 31,		
(in millions)	**2013**	**2012**	**2011**
Income tax (benefit) expense	($42)	$381	$272
Tax effect of changes in OCI	(194)	125	89
Total comprehensive income tax (benefit) expense	($236)	$506	$361

Components of income tax (benefit) expense are as follows:

(in millions)	**Current**	**Deferred**	**Total**
Year Ended December 31, 2013			
U.S. federal	$3	($47)	($44)
State and local	8	(6)	2
Total	$11	($53)	($42)
Year Ended December 31, 2012			
U.S. federal	$19	$269	$288
State and local	56	37	93
Total	$75	$306	$381
Year Ended December 31, 2011			
U.S. federal	($22)	$220	$198
State and local	42	32	74
Total	$20	$252	$272

The effective income tax rate differed from the U.S. federal income tax rate of 35% in 2013, 2012 and 2011 as follows:

	Years Ended December 31,					
	2013		2012		2011	
(dollars in millions)	Amount	Rate	Amount	Rate	Amount	Rate
U.S. Federal income (benefit) expense and tax rate	($1,214)	35.00%	$359	35.00%	$270	35.00%
Increase (decrease) resulting from:						
Goodwill Impairment	1,217	(35.09)	—	—	—	—
State and local income taxes (net of federal benefit)	1	(0.03)	61	5.93	48	6.24
Changes in uncertain tax positions	—	—	—	0.01	(1)	(0.07)
Bank-owned life insurance	(17)	0.50	(18)	(1.76)	(17)	(2.21)
Tax-exempt interest	(13)	0.37	(12)	(1.14)	(10)	(1.23)
Low income housing partnerships	(11)	0.32	(8)	(0.76)	(7)	(0.93)
Other	(5)	0.14	(1)	(0.10)	(11)	(1.47)
Total income tax (benefit) expense and rate	($42)	1.21%	$381	37.18%	$272	35.33%

The decrease in the effective rate from 2012 to 2013 represents the tax rate impact of the 2013 goodwill impairment in addition to the tax rate impact of a 2012 state tax settlement. The state tax settlement represents 2.45% of the total tax rate for 2012 and is included in the rate reconciliation as a component of state and local income taxes (net of federal benefit).

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities are presented below:

(in millions)	December 31, 2013	December 31, 2012
Deferred tax assets:		
Unrealized net loss on securities and derivatives	$397	$203
Allowance for credit losses	475	486
Net operating loss carryforwards	129	266
Accrued expenses not currently deductible	149	150
Investment and other tax credit carryforwards	62	47
Deferred income	35	23
Fair value marks	30	23
Other	—	3
Total deferred tax assets	1,277	1,201
Valuation allowance	(137)	(163)
Deferred tax assets, net of valuation allowance	1,140	1,038
Deferred tax liabilities:		
Leasing transactions	811	739
Amortization of intangibles	296	572
Depreciation	124	95
Pension	56	47
MSRs	50	31
Other	2	—
Total deferred tax liabilities	1,339	1,484
Net deferred tax liability	$199	$446

Certain 2012 balances in the table above were restated to better conform to the current year presentation. This adjustment expanded the pension category to include other employee compensation plans which were included as accrued expenses not currently deductible in 2012.

At December 31, 2013, the Company had deferred tax assets of $191 million in connection with federal and state net operating loss and credit carryforwards. At December 31, 2013, the federal net operating loss carryforward was approximately $19 million, the state net operating loss carryforward was approximately $110 million, federal tax credit carryforwards were approximately $55 million and state tax credit carryforwards were approximately $7 million. These net operating losses and credits will expire, if not utilized, in the years 2014 through 2033, except for approximately $129 thousand of federal alternative minimum tax credits which do not expire.

The Company had at December 31, 2013, a valuation allowance of $137 million against the deferred tax assets related to certain state temporary differences, net operating losses and credits as it is management's current assessment that it is more likely than not that the Company will not recognize a portion of the deferred tax asset related to these items. The valuation allowance decreased $26 million during the year ended December 31, 2013.

Effective with fiscal year ended September 30, 1997, the reserve method for bad debts was no longer permitted for tax purposes. The repeal of the reserve method required the recapture of the reserve balance in excess of certain base year reserve amounts attributable to years ended prior to 1988. At December 31, 2013 the Company's base year loan loss reserves attributable to years ended prior to 1988 for which no deferred income taxes have been provided was $557 million. This base year reserve may become taxable if certain distributions are made with respect to the stock of the Company or if the Company ceases to qualify as a bank for tax purposes. No actions are planned which would cause this reserve to become wholly or partially taxable.

The Company files income tax returns in the U.S. federal jurisdiction and various state and local jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal or state and local income tax examinations by major tax authorities for years before 2008.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows:

(in millions)	December 31, 2013	December 31, 2012	December 31, 2011
Balance at the beginning of the period, January 1	$34	$136	$104
Gross increases for tax positions related to prior years	—	29	48
Gross decreases for tax positions related to prior years	—	—	(6)
Decreases for tax positions relating to settlements with taxing authorities	(1)	(134)	(10)
Gross increases for tax positions related to the current years	—	3	—
Balance at end of period	$33	$34	$136

Included in the total amount of unrecognized tax benefits at December 31, 2013, are potential benefits of $23 million that, if recognized, would affect the effective tax rate.

The Company classifies interest and penalties related to unrecognized tax benefits as a component of income taxes. The Company accrued $2 million, $14 million, and $18 million of interest expense through December 31, 2013, 2012, and 2011, respectively. The Company had approximately $14 million, $12 million, and $55 million accrued for the payment of interest at December 31, 2013, 2012, and 2011, respectively. There were no amounts accrued for penalties as of December 31, 2013, 2012, and 2011, and there were no penalties recognized during 2013, 2012, and 2011.

It is anticipated that during 2014 the Company will enter into settlement agreements with certain state taxing authorities regarding the issue of nexus. Settlement of these uncertainties would reduce the unrecognized tax benefit by $19 million. During 2012, the Company settled a state tax issue for the years 2003 through 2008 related to its real estate investment trust and various passive investment companies. Settlement of these uncertainties reduced the unrecognized tax benefit by $134 million.

NOTE 15 - DERIVATIVES

In the normal course of business, the Company enters into a variety of derivative transactions in order to meet the financing needs of its customers and to reduce its own exposure to fluctuations in interest rates and foreign currency exchange rates. The Company does not use derivatives for speculative purposes.

The Company's derivative instruments are recognized on the Consolidated Balance Sheets at fair value. Information regarding the valuation methodology and inputs used to estimate the fair value of the Company's derivative instruments is described in Note 19 "Fair Value Measurements".

The following table identifies derivative instruments included on the Consolidated Balance Sheets in derivative assets and derivative liabilities:

	December 31, 2013			December 31, 2012		
(in millions)	Notional Amount[1]	Derivative assets	Derivative liabilities	Notional Amount[1]	Derivative assets	Derivative liabilities
Derivatives designated as hedging instruments:						
Interest rate swaps	$5,500	$23	$412	$4,200	$1	$257
Derivatives not designated as hedging instruments:						
Interest rate swaps	29,355	654	558	31,227	1,102	1,033
Foreign exchange contracts	7,771	94	87	5,978	71	67
Other contracts	569	7	10	2,815	35	15
Total derivatives not designated as hedging instruments		755	655		1,208	1,115
Gross derivative fair values		$778	$1,067		$1,209	$1,372
Less: Gross amounts offset in the Consolidated Balance Sheets[2]		(128)	(128)		(54)	(54)
Total net derivative fair values presented in the Consolidated Balance Sheets[3]		$650	$939		$1,155	$1,318

[1] The notional or contractual amount of interest rate derivatives and foreign exchange contracts is the amount upon which interest and other payments under the contract are based. For interest rate derivatives, the notional amount is typically not exchanged. Therefore, notional amounts should not be taken as the measure of credit or market risk as they tend to greatly overstate the true economic risk of these contracts.

[2] Amounts represent the impact of legally enforceable master netting agreements that allow the Company to settle positive and negative positions.

[3] The Company also offsets assets and liabilities associated with repurchase agreements on the Consolidated Balance Sheets. See Note 3 - Securities for further information.

The Company's derivative transactions are internally divided into three sub-groups: institutional, customer and residential loan.

Institutional derivatives

The institutional derivatives portfolio primarily consists of interest rate swap agreements that are used to hedge the interest rate risk associated with the Company's investment securities, loans and financing liabilities (i.e. borrowed funds, deposits, etc.). The goal of the Company's interest rate hedging activities is to manage interest rate sensitivity so that movements in interest rates do not significantly adversely affect net interest income.

The Company enters into certain interest rate swap agreements to hedge the market risk associated with fixed income securities. By entering into "plain vanilla" pay-fixed / receive-floating interest rate swaps, the Company is able to minimize the variability in the fair value of these securities due to changes in interest rates. The Company also enters into certain interest rate swap agreements to hedge the interest rate risk associated with floating rate loans. By entering into pay-floating / receive-fixed interest rate swaps, the Company is able to minimize the variability in the cash flows of these assets due to changes in interest rates. The Company also enters into certain interest rate swap agreements designed to hedge a portion of the Company's borrowed funds and deposits. By entering into a pay-fixed / receive-floating interest rate swap, a portion of these liabilities is effectively converted to a fixed rate liability for the term of the interest rate swap agreement.

Customer derivatives

The customer derivatives portfolio consists of interest rate swap agreements and option contracts that are transacted to meet the financing needs of the Company's customers. Offsetting swap and cap agreements are simultaneously transacted to effectively eliminate the Company's market risk associated with the customer derivative products. The customer derivatives portfolio also includes foreign exchange contracts that are entered into on behalf of customers for the purpose of hedging exposure related to cash orders and loans and deposits denominated in foreign currency. The primary risks associated with these transactions arise from exposure to changes in foreign currency exchange rates and the ability of the counterparties to meet the terms of the contract. To manage this market risk, the Company simultaneously enters into offsetting foreign exchange contracts.

Residential loan derivatives

The Company enters into residential loan commitments that allow residential mortgage customers to lock in the interest rate on a residential mortgage while the loan undergoes the underwriting process. The Company also uses forward sales contracts to protect the value of residential mortgage loans and loan commitments that are being underwritten for future sale to investors in the secondary market.

The Company has certain derivative transactions that are designated as hedging instruments described as follows:

Derivatives designated as hedging instruments

The majority of the Company's institutional hedging portfolio qualifies for hedge accounting. This includes interest rate swaps that are designated in highly effective cash flow hedging relationships. The Company formally documents at inception all hedging relationships, as well as risk management objectives and strategies for undertaking various accounting hedges. Additionally, the Company uses dollar offset or regression analysis at the hedge's inception, and at least quarterly thereafter to assess whether the derivatives are expected to be, or have been, highly effective in offsetting changes in the hedged item's expected cash flows. The Company discontinues hedge accounting when it is determined that a derivative is not expected to be or has ceased to be effective as a hedge, and then reflects changes in fair value in earnings after termination of the hedge relationship.

Cash flow hedges

The Company enters into certain interest rate swap agreements designed to hedge a portion of the Company's floating rate assets and financing liabilities (including its borrowed funds and deposits). All of these swaps have been deemed as highly effective cash flow hedges. The effective portion of the hedging gains and losses associated with these hedges are recorded in OCI; the ineffective portion of the hedging gains and losses is recorded in earnings (other income). Hedging gains and losses on derivative contracts reclassified from OCI to current period earnings are included in the line item in the accompanying consolidated statements of operations in which the hedged item is recorded, and in the same period that the hedged item affects earnings. During the next 12 months, approximately $46 million of net loss (pre-tax) on derivative instruments included in OCI is expected to be reclassified to net interest expense in the Consolidated Statements of Operations

Hedging gains and losses associated with the Company's cash flow hedges are immediately reclassified from OCI to current period earnings (other net gains) if it becomes probable that the hedged forecasted transactions will not occur by the originally specified time period.

The following table summarizes certain information related to the Company's cash flow hedges:

The Effect of Cash Flow Hedges on Net Income and Stockholder's Equity

	Amounts Recognized for the Years Ended		
(in millions)	December 31, 2013	December 31, 2012	December 31, 2011
Effective portion of gain (loss) recognized in OCI[1]	($59)	($42)	($177)
Amounts reclassified from OCI to interest income[2]	56	—	—
Amounts reclassified from OCI to interest expense[2]	(235)	(335)	(517)
Amounts reclassified from OCI to net gains[3]	(1)	(1)	—
Ineffective portion of gain recognized in other income[4]	—	1	—

[1] The cumulative effective gains and losses on the Company's cash flow hedging activities are included on the AOCI line item on the Consolidated Balance Sheets.

[2] This amount includes both (a) the amortization of effective gains and losses associated with the Company's terminated cash flow hedges and (b) the current reporting period's interest settlements realized on the Company's active cash flow hedges. Both (a) and (b) were previously included on the accumulated other comprehensive loss line item on the Consolidated Balance Sheets and were subsequently recorded as adjustments to the interest expense of the underlying hedged item.

[3] This amount represents hedging gains and losses that have been immediately reclassified from accumulated other comprehensive loss based on the probability that the hedged forecasted transactions would not occur by the originally specified time period. This amount is reflected in the other net gains (losses) line item on the Consolidated Statements of Operations.

[4] This amount represents the net ineffectiveness recorded during the reporting periods presented plus any amounts excluded from effectiveness testing. These amounts are reflected in the other income line item on the Consolidated Statements of Operations.

Economic Hedges

The Company's customer derivatives are recorded on the Consolidated Balance Sheets at fair value. These include interest rate and foreign exchange derivative contracts that are transacted to meet the hedging and financing needs of the Company's customers. Mark-to-market adjustments to the fair value of customer related interest rate contracts are included in other income in the accompanying Consolidated Statements of Operations. Mark-to-market adjustments to the fair value of foreign exchange contracts relating to foreign currency loans are included in interest and fees on loans and leases in the accompanying Consolidated Statements of Operations, while all other foreign currency contract fair value changes are included in international fees. In both cases, the mark-to-market gains and losses associated with the customer derivatives are mitigated by the mark-to-market gains and losses on the offsetting interest rate and foreign exchange derivative contracts transacted.

The Company's residential loan derivatives (including residential loan commitments and forward sales contracts) are recorded on the Consolidated Balance Sheets at fair value. Mark-to-market adjustments to the fair value of residential loan commitments and forward sale contracts are included in noninterest income under mortgage banking.

The following table summarizes certain information related to the Company's economic hedges:

The Effect of Customer Derivatives and Economic Hedges on Net Income

	Amounts Recognized in Noninterest Income for the Years Ended December 31,		
(in millions)	2013	2012	2011
Customer derivative contracts			
Customer interest rate contracts[1]	$79	$292	$706
Customer foreign exchange contracts[1]	18	10	2
Residential loan commitments[3]	(7)	11	(28)
Economic hedges			
Offsetting derivatives transactions to hedge interest rate risk on customer interest rate contracts[1]	(30)	(285)	(690)
Offsetting derivatives transactions to hedge foreign exchange risk on customer foreign exchange contracts[2]	(15)	(10)	(1)
Forward sale contracts[3]	25	8	22
Total	$70	$26	$11

[1] Reported in customer derivatives on the Consolidated Statements of Operations.

[2] Reported in international fees on the Consolidated Statements of Operations.

[3] Reported in mortgage banking on the Consolidated Statements of Operations.

NOTE 16 - COMMITMENTS, GUARANTEES AND CONTINGENCIES

Commitments

Commitments to extend credit are agreements to lend to customers in accordance with conditions contractually agreed upon in advance. Generally, the commitments have fixed expiration dates or termination clauses and may require payment of a fee. Since many of these commitments are expected to expire without being drawn upon, the contract amounts are not necessarily indicative of future cash requirements.

When-issued securities are agreements to purchase securities that have been authorized for issuance but not yet issued. The fair value of when-issued securities is reflected in the consolidated balance sheets at trade date.

During 2003, the Company entered into a 25-year agreement to acquire the naming and marketing rights of a baseball stadium in Pennsylvania. The Company paid $3 million in each of the years ended December 31, 2013, 2012, and 2011, and is obligated to pay $54 million over the remainder of the contract.

Letters of Credit

Standby letters of credit, both financial and performance, are issued by the Company for its customers. They are used as conditional guarantees of payment to a third party in the event the customer either fails to make specific payments (financial) or fails to complete a specific project (performance). Commercial letters of credit are used to facilitate the import of goods. The commercial letter of credit is used as the method of payment to the Company's customers' suppliers. The Company's exposure to credit loss in the event of counterparty nonperformance in connection with the above instruments is represented by the contractual amount of those instruments, net of the value of collateral held. Standby letters of credit and commercial letters of credit are issued for terms of up to ten years and one year, respectively.

Generally, letters of credit are collateralized by cash, accounts receivable, inventory or investment securities. Credit risk associated with letters of credit is considered in determining the appropriate amounts of reserves for unfunded commitments.

The Company recognizes a liability on the consolidated balance sheets representing its obligation to stand ready to perform over the term of the standby letters of credit in the event that the specified triggering events occur. The liability for these guarantees at December 31, 2013 and 2012 is $3 million and $4 million, respectively.

Risk Participation Agreements

RPAs are guarantees issued by the Company to other parties for a fee, whereby the Company agrees to participate in the credit risk of a derivative customer of the other party. Under the terms of these agreements, the "participating bank" receives a fee from the "lead bank" in exchange for the guarantee of reimbursement if the customer defaults on an interest rate swap. The interest rate swap is transacted as such that any and all exchanges of interest payments (favorable and unfavorable) are made between the lead bank and the customer. In the event that an early termination of the swap occurs and the customer is unable to make a required close out payment, the participating bank assumes that obligation and is now required to make this payment.

RPAs where the Company acts as the lead bank are referred to as "participations-out", in reference to the credit risk associated with the customer derivatives being transferred out of the Company. Participations-out generally occur concurrently with the sale of new customer derivatives. RPAs where the Company acts as the participating bank are referred to as "participations-in", in reference to the credit risk associated with the counterparty's derivatives being assumed by the Company. The Company's maximum credit exposure is based on its proportionate share of the settlement amount of the referenced interest rate swap. Settlement amounts are generally calculated based on the fair value of the swap plus outstanding accrued interest receivables from the customer. The Company's estimate of the credit exposure associated with its risk participations-in as of December 31, 2013 and 2012 is $17 million and $30 million, respectively. The current amount of credit exposure is spread out over 71 counterparties. RPAs generally have terms ranging from 1-5 years; however certain outstanding agreements have terms as long as 9 years.

Other Guarantees

The Company has issued a guarantee to RBS, for a fee, whereby the Company will absorb credit losses related to the sale of option contracts by RBS to customers of the Company. There were outstanding option contracts with a notional value of $2 million and $222 million at December 31, 2013 and 2012, respectively.

The following is a summary of outstanding off balance sheet arrangements:

(in millions)	December 31, 2013	December 31, 2012
Commitment amount:		
Undrawn commitments to extend credit	$53,987	$50,507
Financial standby letters of credit	2,556	3,082
Performance letters of credit	149	152
Commercial letters of credit	64	103
Marketing rights	54	57
Risk participation agreements	17	30
Residential mortgage loans sold with recourse	13	17
Total	$56,840	$53,948

Contingencies

The Company operates in a legal and regulatory environment that exposes RBS Citizens to potentially significant risks. A certain amount of litigation ordinarily results from the nature of the Company's banking and other businesses. The Company is a party to legal proceedings, including class actions. It is also the subject of investigations, reviews, and regulatory matters arising out of its normal business operations, which, in some instances, relate to concerns about unfair and / or deceptive practices and mis-selling of certain products. In addition, the Company engages in discussions with relevant governmental and regulatory authorities on an ongoing and regular basis regarding various issues, and it is possible that any issues discussed or identified may result in investigatory or other action being taken. Litigation and regulatory matters may result in settlements, damages, fines, public or private censure, increased costs, required remediation, restriction on business activities, or other impact on the Company.

In these disputes and proceedings, the Company contests liability and the amount of damages as appropriate. Given their complex nature, it may be years before some of these matters are finally resolved. Moreover, before liability can be reasonably estimated for a claim, numerous legal and factual issues may need to be examined, including through potentially lengthy discovery and determination of important factual matters, and by addressing novel or unsettled legal issues relevant to the proceedings in question.

The Company cannot predict with certainty if, how, or when such claims will be resolved or what the eventual settlement, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages. The Company recognizes a provision for a claim when, in the opinion of management after seeking legal advice, it is probable that a liability exists and the amount of loss can reasonably be estimated. In many proceedings, however, it is not possible to determine whether any loss is probable or to estimate the amount of any loss. In each of the matters described below, the Company is unable to reliably estimate the liability in excess of any provision accrued, if any, that might arise or its effects on the Company's Consolidated Statements of Operations or Consolidated Cash Flows in any particular period.

Set out below are descriptions of significant legal matters involving the Company. Based on information currently available, the advice of legal and other counsel, and established reserves, management believes that the aggregate liabilities, if any, arising from these proceedings will not have a materially adverse effect on the Company's Consolidated Financial Statements.

Fair Labor Standards Act Litigation

The Company has been named in several purported class actions brought under the FLSA and equivalent state statutes alleging that certain categories of branch employees were denied overtime for hours worked. These suits are brought by current and former branch employees alleging that either: (1) they are / were in Assistant Branch Manager positions and were improperly classified as exempt under the FLSA thereby denying them pay for all hours worked, including overtime pay; or (2) they are / were properly classified as non-exempt tellers, bankers or the like but were told not to record all of their hours, had hours they entered deleted by their managers and / or were otherwise denied pay for hours worked, including overtime pay. These cases cover the Company's entire thirteen state footprint, and they have been settled in principle, subject to court approval. Separately, the Company has been named in two lawsuits brought by current and former mortgage loan officers and home loan advisors alleging that they were improperly classified as exempt under the FLSA and corresponding state laws and therefore denied pay for all hours worked, including overtime pay. These cases have been settled, and final court approval of the settlements was granted on January 29, 2014.

Mortgage Repurchase Demands

The Company is an originator and servicer of residential mortgages and routinely sells such mortgage loans in the secondary market and to government-sponsored entities. In the context of such sales, the Company makes certain representations and warranties regarding the characteristics of the underlying loans and, as a result, may be contractually required to repurchase such loans or indemnify certain parties against losses for certain breaches of those representations and warranties. Between the start of January 2009 and the end of December 2013, the Company has received approximately $119 million in repurchase demands and $89 million in indemnification payment requests in respect of loans originated, for the most part, since 2003. Of those claims presented, $64 million was paid to repurchase residential mortgage loans, and $25 million was incurred for indemnification costs to make investors whole. The Company repurchased mortgage loans totaling $35 million and $13 million for the twelve months ended December 31, 2013 and 2012, respectively. The Company incurred indemnification costs of $12 million and $5 million for the twelve months ended December 31, 2013 and 2012, respectively. The Company cannot estimate what the future level of repurchase demands will be or the Company's ultimate exposure, and cannot give any assurance that the historical experience will continue in the future. It is possible that the volume of repurchase demands will increase.

MERS Cases

Counties in four states are plaintiffs in suits against MERSCORP, Inc., MERS and its shareholder financial institutions, including the Company, for its origination and securitization of mortgage loans using the MERS system. The plaintiffs allege that by registering properties in MERS' name the banks fail to pay recording fees as required by state law when properties are transferred among them. Complaints have been dismissed in two states with one such dismissal being affirmed by U.S. Court of Appeals for the Seventh Circuit and the other subject to a motion for reconsideration. The other cases continue. The Company is vigorously defending these matters.

LIBOR Litigation

The Company is a defendant in lawsuits in which allegations have been made that its parent company, RBS Group, manipulated U.S. dollar LIBOR to the detriment of the plaintiffs. The lawsuits include a purported class action on behalf of borrowers of the Company whose interest rate was tied to U.S. dollar LIBOR. The Company is vigorously defending these matters.

Foreclosure-Related Expenses

In May 2013, the civil division of the U.S. Attorney's Office for the Southern District of New York served a subpoena pursuant to the Financial Institutions Reform, Recovery and Enforcement Act of 1989 seeking information regarding home mortgage foreclosure expenses submitted for reimbursement to the United States Department of Housing and Urban Development, FNMA, or FHLMC. The Company is cooperating with the investigation.

Consumer Products

The activities of the Company's bank subsidiaries are subject to extensive laws and regulations concerning unfair or deceptive acts or practices in connection with customer products. Certain of the bank subsidiaries' practices with respect to overdraft protection and other consumer products have not met applicable standards. The bank subsidiaries have implemented and are continuing to implement changes to bring their practices in conformity with applicable laws and regulations. In April 2013, the bank subsidiaries consented to the issuance of orders by the OCC and the FDIC (the Consent Orders). In the Consent Orders (which are publicly available and will remain in effect until terminated by the regulators), the bank subsidiaries neither admitted nor denied the regulators' findings that they had engaged in deceptive marketing and implementation of the bank's overdraft protection program, checking rewards programs, and stop-payment process for pre-authorized recurring electronic fund transfers. The Consent Orders require the bank subsidiaries to pay a total of $10 million in civil monetary penalties, to develop plans to provide restitution to affected customers (the amount of which is anticipated to be approximately $8 million), to cease and desist any operations in violation of Section 5 of the Federal Trade Commission Act, and to submit to the regulators periodic written progress reports regarding compliance with the Consent Orders. In addition, RBS Citizens, N.A. agreed to take certain remedial actions to improve its compliance risk management systems and to create a comprehensive action plan designed to achieve compliance with the Consent Order. Restitution plans have been prepared and submitted for approval and RBS Citizens, N.A. has submitted for approval, and is in the process of implementing, its action plan for compliance with the Consent Order, as well as updated policies, procedures, and programs related to its compliance risk management systems.

The Company's bank subsidiaries have also identified issues regarding, among other things, certain identity theft and debt cancellation products, certain overdraft fees, the bank subsidiaries' policies and practices with respect to identifying and correcting errors in customer deposits, and the charging of cost-based credit card late payment fees. The bank subsidiaries have paid restitution, or expect to pay restitution, to certain affected customers in connection with certain of these practices. In addition, the bank subsidiaries could face formal administrative enforcement actions from their federal supervisory agencies, including the assessment of civil monetary penalties and restitution, relating to the past practices and policies identified above and other consumer products, and they could face potential civil litigation. The Company does not expect that the aggregate of amounts paid in connection with these matters will have a material adverse effect on the Company's business, financial condition and results of operations.

NOTE 17 - DIVESTITURES AND BRANCH ASSETS AND LIABILITIES HELD FOR SALE

In January 2014, the Company reached an agreement to sell its Chicago-area retail branches, small business operations and select middle market relationships. The sale included 94 branches, approximately $5.3 billion in local deposits and $1.1 billion of locally originated loans as well as related branch premises. The transaction is subject to regulatory approval and is anticipated to close in the second quarter of 2014. As a result of this transaction, the assets and liabilities related to the franchise being sold have been classified as held for sale.

The following table presents the assets and liabilities held for sale related to this transaction as of:

(in millions)	December 31, 2013
Loans held for sale	
Commercial	$551
Commercial real estate	49
Total commercial	600
Residential mortgages	389
Other secured retail	7
Unsecured retail	82
Total retail	478
Total loans held for sale	1,078
Other branch assets held for sale:	
Properties and equipment, net	46
Total other branch assets held for sale	46
Total branch assets held for sale	$1,124
Deposits held for sale	
Demand	$1,020
Checking with interest	849
Regular savings	504
Money market accounts	2,013
Term deposits	891
Total deposits held for sale	$5,277
Total branch liabilities held for sale	$5,277

On June 22, 2012, the Company completed the sale of 57 branches in New York. Assets and deposits totaled $16 million and $325 million, respectively. A gain of $4 million was recognized in other net gains, offset by approximately $4 million in one-time costs recognized in noninterest expense.

In June 2012, the Company entered into a series of transactions to sell substantially all of its venture capital investments. As a result, the Company de-recognized $48 million of assets and recognized losses of $14 million on the transactions which are presented in other net gains in the accompanying Consolidated Statements of Operations.

NOTE 18 - RELATED PARTY TRANSACTIONS

The following is a summary of inter-company borrowed funds:

(dollars in millions)	Related Party	Interest Rate	Maturity Date	December 31, 2013	December 31, 2012
Subordinated debt	RBS	4.961%	January 2024	$334	$0
	RBSG	4.771%	October 2023	333	—
	RBSG	5.158%	June 2023	333	—
	RBS	Three month LIBOR + 1.50%	March 2035	—	289

The Company maintained a $50 million revolving line of credit at December 31, 2013 and 2012 with RBS. This line of credit was not drawn upon at December 31, 2013 or 2012, expired on January 31, 2014, and was not renewed.

The Company enters into interest rate swap agreements with RBS for the purpose of reducing the Company's exposure to interest rate fluctuations. As of December 31, 2013, the total notional amount of swaps outstanding was $5.5 billion which pay fixed rates ranging from 1.78% to 5.47% and receive overnight fed funds rate and one month LIBOR with maturities from 2014 through 2023. Included in this balance were $4 billion of receive-fixed swaps that had been executed as of June 30, 2013 as part of a new hedging program implemented during the quarter ended March 31, 2013. As of December 31, 2012, the total notional amount of swaps outstanding was $4.2 billion which pay fixed rates ranging from 2.94% to 5.47% and receive overnight Federal funds rate with maturities from 2013 through 2016.

In order to meet the financing needs of its customers, the Company enters into interest rate swap and cap agreements with its customers and simultaneously enters into offsetting swap and cap agreements with RBS. The Company earns a spread equal to the difference between rates charged to the customer and rates charged by RBS. The notional amount of these interest rate swap and cap agreements outstanding with RBS was $13.4 billion and $16.0 billion at December 31, 2013 and December 31, 2012, respectively.

Also to meet the financing needs of its customers, the Company enters into a variety of foreign currency denominated products, such as loans, deposits and foreign exchange contracts. To manage the foreign exchange risk associated with these products, the Company simultaneously enters into offsetting foreign exchange contracts with RBS. The Company earns a spread equal to the difference between rates charged to the customer and rates charged by RBS. The notional amount of foreign exchange contracts outstanding with RBS was $4.6 billion and $3.4 billion at December 31, 2013 and December 31, 2012, respectively.

The Company has issued a guarantee to RBS for a fee, whereby the Company will absorb credit losses related to the sale of option contracts by RBS to customers of the Company. There were outstanding option contracts with a notional value of $2 million and $222 million at December 31, 2013 and December 31, 2012, respectively.

Net expense recorded for amounts due to RBS for the years ended December 31, 2013, 2012, and 2011 totaled $592 million, $739 million, and $973 million, respectively.

The Company receives income for providing services and referring customers to RBS. The Company also shares office space with certain RBS entities for which rent expense and / or income is recorded in occupancy expense. The total fee income, net of occupancy expense, for the years ended December 31, 2013, 2012, and 2011 was $26 million, $28 million, and $24 million, respectively. In 2013 the Company paid $1.0 billion of common stock dividends to RBS as part of the exchange transactions described in the Capital Resources section of the MD&A and $185 million of regular dividends to RBS. In 2012, the Company paid $150 million in regular common stock dividends to RBS. There were no dividends paid in 2011.

The Company, as a matter of policy and during the ordinary course of business with underwriting terms similar to those offered to the public, has made loans to directors and executive officers and their immediate families, as well as their affiliated companies. Such loans amounted to $78 million and $92 million at December 31, 2013 and 2012, respectively.

NOTE 19 – FAIR VALUE MEASUREMENTS

As discussed in Significant Accounting Policies, the Company measures or monitors many of its assets and liabilities on a fair value basis. Fair value is used on a recurring basis for assets and liabilities for which fair value is the required or elected measurement basis of accounting. Additionally, fair value is used on a nonrecurring basis to evaluate assets for impairment or for disclosure purposes. Nonrecurring fair value adjustments typically involve the application of lower of cost or market accounting or write-downs of individual assets. The Company also applies the fair value measurement guidance to determine amounts reported for certain disclosures in this note for assets and liabilities not required to be reported at fair value in the financial statements.

Fair Value Option, Residential Mortgage Loans Held for Sale

The Company elected to account for residential mortgage loans held for sale at fair value. Applying fair value accounting to the residential mortgage loans held for sale better aligns the reported results of the economic changes in the value of these loans and their related hedge instruments.

The fair value of residential loans held for sale is derived from observable mortgage security prices and includes adjustments for loan servicing value, agency guarantee fees, and other loan level attributes which are mostly observable in the marketplace. Credit risk does significantly impact the valuation since loans are sold shortly after origination. Therefore, the Company classifies the residential mortgage loans held for sale in Level 2 of the fair value hierarchy.

At December 31, 2013, the fair value carrying amount of residential loans held for sale and the aggregate unpaid principal amount that the Company is contractually entitled to receive at maturity are $176 million and $173 million, respectively. At December 31, 2012, the fair value carrying amount of residential loans held for sale and the aggregate unpaid principal amount that the Company is contractually entitled to receive at maturity were $624 million and $597 million, respectively. The amount of loans past due or nonaccruing is considered insignificant.

The loans accounted for under the fair value option are initially measured at fair value when the financial asset is recognized. Subsequent changes in fair value are recognized in current earnings. The Company recognized $(33) million, $6 million, and $14 million in mortgage banking noninterest income for the years ended December 31, 2013, 2012, and 2011, respectively. Interest income on residential loans held for sale is calculated based on the contractual interest rate of the loan and is recorded in interest income.

Recurring Fair Value Measurements

The Company utilizes a variety of valuation techniques to measure its assets and liabilities at fair value. Following is a description of valuation methodologies used for significant assets and liabilities carried on the balance sheet at fair value on a recurring basis:

<u>Securities AFS:</u> The fair value of securities classified as AFS is based upon quoted prices, if available. Where observable quoted prices are available in an active market, securities are classified as Level 1 in the fair value hierarchy. Classes of instruments that are valued using this market approach include debt securities issued by the U.S. Treasury. If quoted market prices are not available, the fair value for the security is estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. These instruments are classified as Level 2 because they currently trade in active markets and the inputs to the valuations are observable. The pricing models used to value securities generally begin with market prices (or rates) for similar instruments and make adjustments based on the unique characteristics of the instrument being valued. These adjustments reflect assumptions made regarding the sensitivity of each security's value to changes in interest rates and prepayment speeds. Classes of instruments that are valued using this market approach include residential and commercial CMOs, specified pool mortgage "pass-through" securities and other debt securities issued by U.S. Government-sponsored entities and state and political subdivisions.

A significant majority of the Company's Level 1 and 2 securities are priced using an external pricing service. The Company verifies the accuracy of the pricing provided by its primary outside pricing service on a quarterly basis. This process involves using a secondary external vendor to provide valuations for the Company's securities portfolio for comparison purposes. Any securities with discrepancies beyond a certain threshold are researched and, if necessary, valued by an independent outside broker.

In certain cases where there is limited activity or less transparency around inputs to the valuation model, securities are classified as Level 3.

<u>Residential loans held for sale:</u> See the Fair Value Option discussion above.

<u>Derivatives:</u> The majority of the Company's derivatives portfolio is comprised of "plain vanilla" interest rate swaps, which are traded in over-the-counter markets where quoted market prices are not readily available. For these interest rate derivatives, fair value is determined utilizing models that use primarily market observable inputs, such as swap rates and yield curves. The pricing models used to value interest rate swaps calculate the sum of each instrument's fixed and variable cash flows, which are then discounted using an appropriate yield curve (i.e. LIBOR or OIS curve) to arrive at the fair value of each swap. The pricing models do not contain a high level of subjectivity as the methodologies used do not require significant judgment. The Company also considers certain adjustments to the modeled price which market participants would make when pricing each instrument, including a credit valuation adjustment that reflects the credit quality of the swap counterparty. The Company incorporates the effect of exposure to a particular counterparty's credit by netting its derivative contracts with the collateral available and calculating a credit valuation adjustment on the basis of the net position with the counterparty where permitted. The determination of this adjustment requires judgment on behalf of Company management; however the total amount of this portfolio-level adjustment is not material to the total fair value of the interest rate swaps in their entirety. Therefore, interest rate swaps are classified as Level 2 in the valuation hierarchy.

The Company's other derivatives include foreign exchange contracts. Fair value of foreign exchange derivatives uses the mid-point of daily quoted currency spot prices. A valuation model estimates fair value based on the quoted spot rates together with interest rate yield curves and forward currency rates. Since all of these inputs are observable in the market, foreign exchange derivatives are classified as Level 2 in the fair value hierarchy.

<u>Venture capital investments:</u> The Company values its venture capital private equity fund investments based on its capital invested in each fund, which is adjusted by management each quarter, if necessary, to arrive at its estimate of fair value. Adjustments for a fund's underlying investments may be based upon comparisons to public companies, industry benchmarks, current financing round pricing, earnings multiples of comparable companies, current operating performance and future expectations, or third party valuations. Since the inputs to the valuation are difficult to independently corroborate in the marketplace, and involve a significant degree of management judgment, venture capital investments are classified as Level 3 in the fair value hierarchy.

The following table presents assets and liabilities measured at fair value including gross derivative assets and liabilities on a recurring basis at December 31, 2013:

(in millions)	Total	Level 1	Level 2	Level 3
Securities available for sale:				
Mortgage-backed securities	$15,945	$0	$15,945	$0
State and political subdivisions	10	—	10	—
Equity securities	25	8	17	—
U.S. Treasury	15	15	—	—
Residential loans held for sale	176	—	176	—
Derivative assets:				
Interest rate swaps	677	—	677	—
Foreign exchange contracts	94	—	94	—
Other contracts	7	—	7	—
Venture capital investments	5	—	—	5
Total assets	$16,954	$23	$16,926	$5
Derivative liabilities:				
Interest rate swaps	$970	$0	$970	$0
Foreign exchange contracts	87	—	87	—
Other contracts	10	—	10	—
Total liabilities	$1,067	$0	$1,067	$0

The following table presents assets and liabilities measured at fair value including gross derivative assets and liabilities on a recurring basis at December 31, 2012:

(in millions)	Total	Level 1	Level 2	Level 3
Securities available-for-sale:				
Mortgage-backed securities	$18,301	$0	$18,301	$0
State and political subdivisions	21	—	21	—
Equity securities	19	7	12	—
U.S. Treasury	15	15	—	—
Residential loans held for sale	624	—	624	—
Derivative assets:				
Interest rate swaps	1,103	—	1,103	—
Foreign exchange contracts	71	—	71	—
Other contracts	35	—	35	—
Venture capital investments	6	—	—	6
Total assets	$20,195	$22	$20,167	$6
Derivative liabilities:				
Interest rate swaps	$1,290	$0	$1,290	$0
Foreign exchange contracts	67	—	67	—
Other contracts	15	—	15	—
Total liabilities	$1,372	$0	$1,372	$0

The changes in Level 3 assets measured at fair value on a recurring basis are summarized as follows:

	Years Ended December 31,		
(in millions)	2013	2012	2011
Balance as of January 1	$6	$57	$64
Purchases, issuances, sales and settlements:			
Purchases	—	1	2
Sales	(4)	(45)	—
Settlements	3	23	—
Other net losses	—	(30)	(9)
Balance as of December 31	$5	$6	$57
Net unrealized gain (loss) included in net income for the year relating to assets held at December 31	$0	($11)	$9

There were no transfers among Levels 1, 2 or 3 during the years ended December 31, 2013, 2012 and 2011.

Nonrecurring Fair Value Measurements

The following valuation techniques are utilized to measure significant assets for which the Company utilizes fair value on a nonrecurring basis:

Impaired Loans: The carrying amount of collateral-dependant impaired loans is compared to the appraised value of the collateral less costs to dispose. Any excess of carrying amount over the appraised value is charged to the ALLL.

MSRs: MSRs do not trade in an active market with readily observable prices. MSRs are classified as Level 3 since the valuation methodology utilizes significant unobservable inputs. At December 31, 2013 the fair value is calculated using the discounted cash flow model , the model which uses assumptions including weighted average life of 5.4 years (range of 1.8 - 7.4 years), weighted average constant prepayment rate of 13% (range of 9.4% - 41.5%) and weighted average discount rate of 10.8% (range of 10.2% - 13.1%). Refer to Significant Accounting Policies in Note 1 and Mortgage Banking in Note 9 for more information.

Foreclosed assets: Foreclosed assets consist primarily of residential properties. Foreclosed assets are carried at the lower of carrying value or fair value less costs to dispose. Fair value is based upon independent market prices or appraised values of the collateral and is classified as Level 2.

Goodwill: Goodwill is valued using unobservable inputs and is classified as Level 3. Fair value is calculated using the present value of estimated future earnings (discounted cash flow method), the model which uses assumptions including discount rate (9.5%), historical projected loss rates (commercial banking 0.44%; retail banking 0.57%), income tax (35%), and capital retention (7%). Refer to Significant Accounting Policies for a description of the goodwill valuation methodology.

Commercial loans held for sale: Commercial loans held for sale consist primarily of syndicated loans not sold at the time of funding. The mark to market is recorded in noninterest income in the Consolidated Statements of Operations.

The following table presents assets and liabilities measured at fair value on a nonrecurring basis and any gains (losses) recorded in earnings:

	Carrying Value at December 31, 2013				Year Ended December 31, 2013
(in millions)	Total	Level 1	Level 2	Level 3	Total Losses
Impaired collateral dependent loans[1]	$74	$0	$74	$0	($83)
MSRs[2]	185	—	—	185	47
Foreclosed real estate[3]	49	—	49	—	(4)
Goodwill[5]	6,876	—	—	6,876	(4,435)

	Carrying Value at December 31, 2012				Year Ended December 31, 2012
(in millions)	Total	Level 1	Level 2	Level 3	Total Losses
Impaired collateral dependent loans[1]	$292	$0	$292	$0	($101)
MSRs[2]	145	—	—	145	(12)
Foreclosed real estate[3]	92	—	92	—	(6)
Commercial loans held for sale[4]	22	—	22	—	—

	Carrying Value at December 31, 2011				Year Ended December 31, 2011
(in millions)	Total	Level 1	Level 2	Level 3	Total Losses
Impaired collateral dependent loans[1]	$488	$0	$488	$0	($118)
MSRs[2]	157	—	—	157	(42)
Foreclosed real estate[3]	116	—	116	—	(7)

[1] In 2013, impaired loans for which collection is dependent on the loan's collateral in the amount of $161 million were written down to $74 million resulting in an impairment charge of $83 million, which was charged to the allowance for loan and lease losses. In 2012, impaired loans for which collection is dependent on the loan's collateral in the amount of $447 million were written down to their fair value of $292 million resulting in an impairment charge of $101 million, which was charged to the allowance for loan and lease losses. In 2011, impaired loans for which collection is dependent on the loan's collateral in the amount of $875 million were written down to their fair value of $488 million resulting in an impairment charge of $118 million, which was charged to the allowance for loan and lease losses. Fair value of the loans was primarily based on the appraised value of the collateral.

[2] In 2013, MSRs totaling $215 million were evaluated for impairment and written down to $185 million, resulting in an impairment recapture (charge) of $47 million and a total cumulative valuation allowance of $23 million. In 2012, MSRs totaling $215 million were evaluated for impairment and written down to $145 million, resulting in an impairment (charge) of $(12) million and a total cumulative valuation allowance of $70 million. In 2011, MSRs totaling $215 million were evaluated for impairment and written down to $157 million, resulting in an impairment charge of $(42) million. The fair value of MSRs was $195 million, $147 million and $155 million at December 31, 2013, 2012, and 2011 respectively.

[3] In 2013, foreclosed real estate accounted for at the lower of cost or fair value less costs to sell was written down to fair value of $49 million, resulting in impairment (recovery) charges of $4 million. In 2012, foreclosed real estate accounted for at the lower of cost or fair value less costs to sell was written down to fair value of $92 million, resulting in impairment charges of $6 million. In 2011, foreclosed real estate accounted for at the lower of cost or fair value less costs to sell was written down to fair value of $116 million, resulting in impairment charges of $7 million.

[4] In 2012, commercial loans held for sale totaled $22 million; cost approximated fair value.

[5] In 2013, Goodwill totaling $11.3 billion was written down to its implied fair value of $6.9 billion, resulting in an impairment charge of $4.4 billion. Fair value of $6.9 billion was valued as of June 30, 2013.

Disclosures about Fair Value of Financial Instruments

Following is a description of valuation methodologies used to estimate the fair value of financial instruments for disclosure purposes (these instruments are not recorded in the financial statements at fair value):

Loans and leases: For loans and leases not recorded at fair value on a recurring basis that are not accounted for as collateral-dependent loans impaired loans, fair value is estimated by using one of two methods: a discounted cash flow method or a securitization method. The discounted cash flow method involves discounting the expected future cash flows using current rates which a market participant would likely use to value similar pools of loans. Inputs used in this method include observable information such as contractual cash flows (net of servicing cost) and unobservable information such as estimated prepayment speeds, credit loss exposures, and discount rates. The securitization method involves utilizing market securitization data to value the assets as if a securitization transaction had been executed. Inputs used include observable market-based MBS data and pricing adjustments based on unobservable data reflecting the liquidity risk, credit loss exposure and other characteristics of the underlying loans. The internal risk weighted balances of loans are grouped by product type for purposes of these estimated valuations. For nonaccruing loans, fair value is estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets. Fair value of collateral-dependent loans is primarily based on the appraised value of the collateral.

Loans held for sale: Balances are loans that were transferred to loans held for sale that are reported at book value.

Securities held to maturity: The fair value of securities classified as HTM is estimated using pricing models, quoted prices of securities with similar characteristics or discounted cash flow. The pricing models used to value these securities generally begin with market prices (or rates) for similar instruments and make adjustments based on the unique characteristics of the instrument being valued. These adjustments reflect assumptions made regarding the sensitivity of each security's value to changes in interest rates and prepayment speeds.

Other investment securities: The cost basis carrying value of other investment securities, such as FHLB stock and FRB stock, is assumed to approximate the fair value of the securities. As a member of the FHLB and FRB, the Company is required to hold FHLB and FRB stock. The stock can be sold only to the FHLB and FRB upon termination of membership, or redeemed at the FHLB's or FRB's sole discretion.

Deposits: The fair value of demand deposits, checking with interest accounts, regular savings and money market accounts is the amount payable on demand at the balance sheet date. The fair value of term deposits is estimated by discounting the expected future cash flows using rates currently offered for deposits of similar remaining maturities.

Deposits held for sale: Balances are deposits that were transferred to held for sale that are reported at book value.

Federal funds purchased and securities sold under agreements to repurchase and borrowed funds: Rates currently available to the Company for debt of similar terms and remaining maturities are used to discount the expected cash flows of existing debt.

The following table is a summary of fair value for financial instruments not recorded at fair value in the Consolidated Financial Statements. The carrying amounts in the following table are recorded in the consolidated balance sheets under the indicated captions:

	December 31, 2013							
	Total		Level 1		Level 2		Level 3	
(in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets:								
Loans and leases	$85,859	$85,724	$0	$0	$74	$74	$85,785	$85,650
Loans held for sale	1,078	1,078	—	—	—	—	1,078	1,078
Securities held to maturity	4,315	4,257	—	—	4,315	4,257	—	—
Other investment securities	935	935	—	—	935	935	—	—
Financial Liabilities:								
Deposits	86,903	86,907	—	—	86,903	86,907	—	—
Deposits held for sale	5,277	5,277	—	—	5,277	5,277	—	—
Federal funds purchased and securities sold under agreements to repurchase	4,791	4,791	—	—	4,791	4,791	—	—
Borrowed funds	3,656	3,654	—	—	3,656	3,654	—	—

	December 31, 2012							
	Total		Level 1		Level 2		Level 3	
(in millions)	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial Assets:								
Loans and leases	$87,248	$86,856	$0	$0	$292	$292	$86,956	$86,564
Other investment securities	1,061	1,061	—	—	1,061	1,061	—	—
Financial Liabilities:								
Deposits	95,148	95,192	—	—	95,148	95,192	—	—
Federal funds purchased and securities sold under agreements to repurchase	3,601	3,601	—	—	3,601	3,601	—	—
Borrowed funds	1,195	1,194	—	—	1,195	1,194	—	—

NOTE 20 - REGULATORY MATTERS

As a BHC, the Company is subject to regulation and supervision by the FRBG. The primary subsidiaries of RBS Citizens are its two insured depository institutions RBS Citizens, N.A., a national banking association whose primary federal regulator is the OCC, and Citizens Bank of Pennsylvania a Pennsylvania-chartered savings bank regulated by the Department of Banking of the Commonwealth of Pennsylvania and supervised by the FDIC as its primary federal regulator. Under the regulatory capital adequacy guidelines of the FDICIA, the Company and its banking subsidiaries must meet specific capital requirements. These requirements are expressed in terms of the following ratios: (1) Risk-based Total Capital (total capital / risk-weighted on-and off-balance sheet assets); (2) Risk-based Tier 1 Capital (tier 1 capital / risk weighted on- and off-balance sheet assets); and Tier 1 Leverage (tier 1 capital / adjusted average quarterly assets). To meet the regulatory capital requirements, the Company and its banking subsidiaries must maintain minimum Risk-based Total Capital, Risk-based Tier 1 Capital, and Tier 1 Leverage ratios. In addition, the Company must not be subject to a written agreement, order or capital directive with any of its regulators. Failure to meet minimum capital requirements can result in the initiation of certain actions that, if undertaken, could have a material effect on the Company's Consolidated Financial Statements.

The following table presents capital and capital ratio information:

			FDIC Requirements			
	Actual		Minimum Capital Adequacy		Classification as Well-capitalized	
(dollars in millions)	Amount	Ratio	Amount	Ratio	Amount	Ratio
As of December 31, 2013						
Total Capital to Risk Weighted Assets	$15,885	16.1%	$7,891	8.0%	$9,863	10.0%
Tier 1 Capital to Risk Weighted Assets	13,301	13.5%	3,945	4.0%	5,918	6.0%
Tier 1 Capital to Average Assets (Leverage)	13,301	11.6%	3,433	3.0%	5,721	5.0%
As of December 31, 2012						
Total Capital to Risk Weighted Assets	$15,623	15.8%	$7,901	8.0%	$9,876	10.0%
Tier 1 Capital to Risk Weighted Assets	14,036	14.2%	3,951	4.0%	5,926	6.0%
Tier 1 Capital to Average Assets (Leverage)	14,036	12.1%	3,475	3.0%	5,791	5.0%

In accordance with federal and state banking regulations, dividends paid by the Company's banking subsidiaries to the Company itself are generally limited to the retained earnings of the respective banking subsidiaries unless specifically approved by the appropriate bank regulator. The Company declared and paid RBS total common stock dividends of $1.2 billion in 2013. There were $150 million in common stock dividends in 2012 and no common stock dividends in 2011.

The earnings impact of goodwill impairment recognized by RBS Citizens, N.A. has put the bank subsidiary in the position of having to request specific approval from the OCC before executing capital distributions to its parent, RBS Citizens. This requirement will be in place through the fourth quarter of 2015. Regardless of the OCC's decision regarding capital distributions by RBS Citizens, N.A., the stand-alone BHC, as of December 31, 2013, has liquid assets in excess of $554 million compared to an annual interest burden on existing subordinated debt of approximately $63 million.

NOTE 21 - SUPPLEMENTAL CASH FLOW INFORMATION

Supplemental cash flow information is as follows:

	Years Ended December 31,		
(in millions)	2013	2012	2011
Supplemental cash flow information:			
Interest paid	$452	$644	$899
Income taxes paid (refunded)	20	201	(109)
Supplemental schedule of non-cash investing and financing activities:			
Transfer of securities from available for sale to held to maturity	$4,240	$0	$0
Transfer of loans held for sale	1,078	22	—
Loans securitized and transferred to securities available for sale	106	21	62
Capital contribution	14	27	30
Accrual and income tax true up related to the 2010 sale of RBS WorldPay, Inc.	—	—	12
Due from broker for securities sold but not settled	(442)	(4)	—
Due to broker for securities purchased but not settled	—	2	—

NOTE 22 - RECLASSIFICATIONS OUT OF ACCUMULATED OTHER COMPREHENSIVE INCOME

The following table presents the changes in the balances, net of taxes, of each component of OCI:

(in millions)	Net Unrealized Gains (Losses) on Derivatives	Net Unrealized Gains (Losses) on Securities	Defined Benefit Pension Plans	Total AOCI
Balance at December 31, 2012	($240)	$306	($378)	($312)
Other comprehensive loss before reclassifications	(172)	(285)	—	(457)
Other than temporary impairment not recognized in earnings on securities	—	(26)	—	(26)
Amounts reclassified from other comprehensive income	114	(86)	119	147
Net other comprehensive income (loss)	(58)	(397)	119	(336)
Balance at December 31, 2013	($298)	($91)	($259)	($648)

The following table reports the amounts reclassified out of each component of OCI and into the Consolidated Statement of Operations:

(in millions)	Year Ended December 31, 2013	
Details about AOCI Components	**Amount Reclassified from AOCI**	**Affected Line Item in the Consolidated Statements of Operations**
Reclassification adjustment for net derivative gains (losses) included in net income (loss):	$56	Interest income
	(235)	Interest expense
	(1)	Other net gains
	(180)	Total before tax
	(66)	Tax benefit
	($114)	Loss, net of tax
Reclassification of net securities gains (losses) to net income (loss):	$144	Net gains on sales of securities available for sale
	(8)	Net impairment losses recognized in earnings
	136	Total before tax
	50	Tax expense
	$86	Income, net of tax
Reclassification of changes related to the employee benefit plan:	($190)	Salaries and employee benefits
	(190)	Total before tax
	(71)	Tax benefit
	($119)	Loss, net of tax
Total reclassification gains (losses)	($147)	Loss, net of tax

The following table presents the effects to net income of the amounts reclassified out of OCI:

(in millions)	Year Ended December 31, 2013
Net interest income (includes ($179) of AOCI reclassifications)	$3,058
Provision for credit losses	479
Noninterest income (includes $135 of AOCI reclassifications)	1,632
Noninterest expense (includes $190 of AOCI reclassifications)	7,679
Income before income tax expense (benefit)	(3,468)
Income tax expense (benefit) (includes $87 income tax net benefit from reclassification items)	(42)
Net income (loss)	($3,426)

NOTE 23 - EXIT COSTS AND RESTRUCTURING RESERVES

The Company continues to review its structural expense base in a company-wide effort to create a more streamlined organization, reduce expense growth, and provide funds for future growth initiatives. During 2013, RBS Citizens introduced branch image capture on the teller line which automated several key processes within the branch network.

The following table includes the activity in the exit costs and restructuring reserves:

(in millions)	Severance	Facilities Costs	Fixed Assets	Other	Total
Reserve balance as of January 1, 2011	$9	$15	$0	$1	$25
Additions	9	43	9	4	65
Utilization	(9)	(6)	(2)	(5)	(22)
Reserve balance as of December 31, 2011	9	52	7	—	68
Additions	2	1	—	4	7
Reversals	(1)	(11)	—	—	(12)
Utilization	(7)	(22)	—	(4)	(33)
Reserve balance as of December 31, 2012	3	20	7	—	30
Additions	6	15	7	3	31
Reversals	(1)	(4)	—	—	(5)
Utilization	(6)	(13)	(8)	(3)	(30)
Reserve balance as of December 31, 2013	$2	$18	$6	$0	$26

In 2013, the Company reversed restructuring charges of $5 million and recorded $31 million in noninterest expense. The reversed restructuring charges consisted primarily of lease termination costs of $4 million, and employee termination benefits of $1 million. The recorded restructuring charges consisted primarily of employee termination benefits of $6 million, lease termination costs of $15 million , fixed asset write-offs of $7 million, and miscellaneous other expense of $3 million.

In the year ended December 31, 2012, the Company recorded a $7 million charge to noninterest expense for other restructuring charges consisting primarily of lease termination costs of $1 million, employee termination benefits of $2 million, and miscellaneous other expense of $4 million.

NOTE 24 - SUBSEQUENT EVENTS

The Company has evaluated events that have occurred subsequent to December 31, 2013 through March 12, 2014, the date the Consolidated Financial Statements were issued. In January 2014, the Company reached an agreement to sell 94 retail branches, including loans, deposits, and related branch premises located in Illinois. The agreement includes the sale of approximately $1.1 billion in loans, $5.3 billion in deposits and related branch premises. The all-cash transaction is expected to close in the second quarter of 2014. As a result of this transaction, the assets and liabilities related to the branches being sold have been classified as held for sale in the Consolidated Balance Sheet at December 31, 2013.

BUSINESS

Overview

RBS Citizens is a BHC and a FHC headquartered in Providence, Rhode Island. Registered under the BHC Act, RBS Citizens is subject to the supervision and regulation of the Federal Reserve. In 1988, RBS Citizens became a wholly-owned subsidiary of RBS Group. By joining RBS Group, RBS Citizens has gained access to certain international resources and support of RBS Group and RBS Group affiliates, including cross-sale of services to meet the needs of the Company's clients. RBS Citizens remains distinct from and independent of the other entities within RBS Group's other businesses in the U.S. and has its own board of directors and executive management team.

The primary subsidiaries of RBS Citizens are its two insured depository institution subsidiaries, RBS Citizens, N.A. and Citizens Bank of Pennsylvania, which it refers to as RBS Citizens' bank subsidiaries. As of December 31, 2013, RBS Citizens was the thirteenth largest BHC in the U.S. in total assets and among the top 10 banking groups in terms of branch and ATM network, based on internal research reports that excluded non-retail banks. As of the same date, RBS Citizens had approximately 19,000 employees, $122 billion in assets, $87 billion in deposits and $86 billion in loans. RBS Citizens' Tier 1 Capital and Total Capital ratios were 13.5% and 16.1%, respectively, as of December 31, 2013.

Through its two bank subsidiaries, RBS Citizens has approximately 1,400 branches and more than 3,500 ATMs as of December 31, 2013. RBS Citizens' core footprint covers twelve states in the New England, Mid-Atlantic and Midwest regions: Connecticut, Delaware, Massachusetts, New Hampshire, New Jersey, New York, Pennsylvania, Rhode Island and Vermont, and with operations under the Charter One brand in Ohio, Michigan and Illinois.

The principal business divisions of RBS Citizens – consumer banking and commercial banking – provide a wide range of retail and commercial banking products and services to consumers and businesses. RBS Citizens aims to provide a complete set of banking products and services, comparable to those offered by national financial services institutions, while distinguishing itself with local delivery and customer service. RBS Citizens' operating philosophy includes a commitment to quality customer service – notably convenience and responsiveness to customer needs and concerns – and to the communities in which it operates.

Competitive Strengths

RBS Citizens believes it has a robust franchise and operates in attractive geographies with significant opportunities. The Company believes its disciplined focus on building meaningful scale and enhancing its competitive position is supported by the following attributes:

- Strong market position in its diversified, demographically attractive geographic markets: RBS Citizens' deposit market share ranks in the top five in eight of its ten major markets, based on the annual FDIC deposit data as of June 30, 2013 shown in the table below. Based on Greenwich Associates' research for December 31, 2013, RBSCFG middle market has a top five rank in customer and lead bank penetration and has a 10% market share in RBSCFG's core footprint. RBSCFG is also ranked fifth in the new capital markets business for middle market customers within the footprint and nationally, based on Thompson Reuter's league tables for December 2013.

The following table depicts RBS Citizens deposit market share metrics as of June 30, 2013:

Markets	Total Active Branches	Traditional Branches	In-store Branches	Total Deposits In Millions	Market Rank	Market Share
Boston	212	137	75	$28,343	2	16.4%
Philadelphia	188	138	50	17,012	4	8.1
Providence	100	60	40	12,854	1	34.6
Pittsburgh	131	81	50	7,130	2	8.8
Chicago	105	97	8	5,999	12	2.0
Detroit	95	78	17	4,563	6	4.6
Cleveland	64	55	9	4,105	5	7.9
Manchester	28	20	8	4,014	1	38.7
Albany	29	17	12	1,590	4	7.1
Buffalo	43	17	26	1,573	4	4.8

*Source: FDIC, June 2013; excludes "non-retail banks" as defined by SNL Financial. The scope of "non-retail banks" is subject to the discretion of SNL Financial, but typically includes: industrial bank and non-depository trust charters, institutions with over 20% brokered deposits (of total deposits), institutions with over 20% credit card loans (of total loans), institutions deemed not to broadly participate in the banking services market, and other non-retail competitor banks of RBS Citizens.

- RBS Citizens' customers are offered the personal service of a local community bank, and the products and conveniences of a national financial services organization. With a local distribution system that consists of approximately 1,400 branches, more than 3,500 ATMs, numerous call centers, online and mobile channels and a corporate culture emphasizing the delivery of a differentiated consumer experience, the Company provides personal and consumer-oriented services to its clients. At the same time, the Company's access to certain resources of RBS Group, including certain capital markets and international cash management services, significant investment in technology and focus on training employees, enable it to provide a wide range of sophisticated products and services at the level of a national financial services organization;

- RBS Citizens' Tier 1 Capital ratio increased from 13.0% as of December 31, 2010 to 13.5% as of December 31, 2013, compared to a peer average of 12.0% and 11.4%, respectively. In terms of asset quality indicators, RBS Citizens' non-performing loans[1] to total loans ratio was 2.52% and 1.59% as of December 31, 2010 and 2013, respectively (such ratios are extracted from U.S. regulatory filings that use different methodologies from U.S. GAAP).

- RBS Citizens' Experienced and Respected Management Team: RBS Citizens has assembled an executive management team that possesses significant depth of knowledge and expertise. Effective October 1, 2013, RBS Citizens underwent a change in leadership as Bruce Van Saun, previously serving as RBS Group's Chief Financial Officer, was named Chairman and Chief Executive Officer of RBS Citizens. Bruce Van Saun has over 30 years of financial services experience and served as the Chief Financial Officer and an Executive Director of the Royal Bank of Scotland Group since October 2009. His substantial experience in the banking industry provides a valuable perspective to RBS Citizens' growth and operating strategies.

  The executive management team has extensive experience supervising consumer and commercial banking, technology, operations, credit and regulatory compliance. Additionally, senior managers in RBS Citizens' commercial and consumer banking divisions have substantial industry experience and extensive networks of contacts, and have served in managerial roles at Fortune 500 financial services companies.

[1]Non-performing loans exclude Restructured loans that are in compliance with their modified terms.

Investments in Technology

In order to deliver value to each group of stakeholders, RBS Citizens is strategically investing in technology infrastructure. RBS Citizens has made approximately $900 million of strategic investments in technology during the past several years to strengthen value proposition, improve efficiencies, and reduce risk. These capital outlays, necessary to prepare the organization for the future, focused on upgrading and replacing older applications and developing new automation capabilities as outlined below. Many of these projects were implemented in 2013.

- **Commercial loan origination and servicing platform:** To reduce errors, improve data quality and enhance controls in support of the credit approval framework, a new commercial loan origination and servicing platform replaced the legacy loan accounting system. The loan servicing component was deployed in fourth quarter of 2012. The roll out of the origination component began during the first quarter of 2013 and was fully implemented by the end of 2013.
- **Auto finance origination system:** To allow selective approval of applications from lower credit tiers and provide pricing with more granularity for those tiers, RBS Citizens implemented a new auto finance origination system in 2013.
- **Home lending origination system:** To retain a competitive and viable position in the current home lending market. RBS Citizens is implementing a home lending origination system with online imaging to replace the current paper-based platform. The new system will also greatly enhance data quality controls, a key component in RBS Citizens ability to continue its participation in the secondary market. Deployment timeline is currently under review.
- **Branch image capture:** To eliminate errors and improve data quality, RBS Citizens has introduced branch image capture on the teller line which automates several key processes within the branch network. Enhanced customer segmentation capability supports RBS Citizens' “know-your-customer” approach, which was deployed in 2013
- **Desktop transformation program:** To reduce risk of data breach by improving access controls and centrally enforcing technology standards and policies, RBS Citizens implemented a desktop transformation program to mirror back office desktop computers to the data centers, creating a “virtual” desktop. More than 8,000 users were enabled to utilize the Virtual Computing Service by the end of 2013.
- **Enterprise data initiative:** To centralize data on a standard platform and provide tools to expand access in support of management and control processes, including risk management, RBS Citizens has established an enterprise data initiative. This initiative focuses on source system data remediation to ensure better quality models, management information and portfolio management capability. Data requirements mandated by the implementation of the DFA are also being prioritized. The first phase of this initiative went live in September 2013.
- **Infrastructure Stability:** To address infrastructure stabilization, scalability, currency and risk mitigation concerns, RBS Citizens has commenced a multi-year infrastructure improvement effort. Upon completion, RBS Citizens will have a safer banking platform, improved recovery capabilities, better IT lifecycle management and enhanced customer experience. The project is being implemented in a phased approach.

Business Strategy

RBS Citizens' long-term goal is to become a top-performing regional bank within its footprint. The objectives in the near-term are to improve financial performance, deliver a differentiated customer experience, and complete the build out of operational capabilities including a robust risk, control, and technology infrastructure. Furthermore, the Company aspires to become a top performing regional bank through the lenses of its five major stakeholders: customers, investors, regulators, colleagues, and communities.

- **Customers:** Recognizing that the Company competes in a highly competitive industry and that good banking is personal, RBS Citizens prepares employees to deliver a consistent, high-quality experience with every customer interaction. The Consumer Banking value proposition is based on providing a simple, clear and personal banking experience. Commercial Banking focuses on providing a client-centric experience based on thought leadership and product capabilities. Substantial investments have been made in colleague training, product capabilities and technology/ infrastructure to strengthen the value proposition in both divisions.

  The Company also strives to ensure customers select RBS Citizens as their primary banking partner by helping them achieve their financial goals and by offering a full range of products and services. The Company's aim is to consistently deliver high-quality services by anticipating customer needs and providing convenient, customer-oriented options and solutions. In 2013, RBS Citizens continued to deepen existing customer relationships by improving and expanding distribution channels (including mobile and ATM offerings), improving product capabilities, increasing cross-sell opportunities, and supplementing capability gaps with select strategic partnerships.

In recognition of RBS Citizens customer experience, *Money Magazine* named it "One of the Nation's Best Banks" in 2013. In addition to a "robust presence" defined by its many branches and ATMs, *Money* recognized RBS Citizens extended branch hours that include seven-day-a-week supermarket branches. *Money* also noted that RBS Citizens convenience options also extend to its mobile banking apps for Android and iPhone, which are generating positive customer feedback in the industry. An August report issued by Xtreme Labs noted that "Citizens Bank is the only bank with the highest rated apps on both Android (4.5 stars) and iOS (4.5 stars) platforms."

- **Investors:** In order to prepare for the upcoming IPO, RBSCFG commenced a number of actions in 2013. These initiatives are expected to improve financial performance; narrow the product, geography and capability gap with its regional peer banks; maximize returns; prepare for separation from RBS Group; and demonstrate positive performance momentum for an upcoming partial IPO.

    - Performance improvement initiatives included:

        - **Treasury Actions:** Starting early in the third quarter of 2013, after a substantial rise in interest rates, RBSCFG initiated a program to expand its investment portfolio by purchasing mortgage-backed securities ($5.5 billion of agency and $2.3 billion of non-agency inventory) and high-quality jumbo mortgages ($2.0 billion). As of December 31, 2013, executed program balances stood at $3.7 billion of agency, $1.3 billion of non-agency and $1.1 billion of jumbo mortgages.

        - **Consumer Banking:** There are a number of ongoing mortgage loan initiatives. For example, the strategy to sell conforming mortgages to the agencies has been changed to instead retain a greater percentage of them on the balance sheet. The Consumer business also hired additional loan officers to support plans to increase jumbo origination volumes. These actions should serve to offset some of the predicted slowdown in mortgage originations. In addition, the Consumer business is evaluating potential loan-flow production arrangements, particularly in Auto and Student Lending.

        - **Commercial Banking:** Commercial Banking is developing scale and expertise in targeted products, channels and industries to strengthen client relationships and reduce risk. Commercial initiatives include focused expansion in the mid-corporate market, healthcare and technology verticals, institutional commercial real estate, franchise finance, and asset-based lending businesses through the build out of relationship, portfolio and credit managers.

        - **Tax Rate Optimization:** RBSCFG is utilizing low-income housing tax benefits and is evaluating tax-efficient sustainable energy options in order to improve its effective tax rate.

        - **Capital Actions:** RBSCFG will continue taking steps to further optimize its capital structure (i.e. exchange excess common equity for alternative forms of regulatory capital) to improve returns.

    - RBSCFG launched a special initiative called Project "TOP", which stands for tapping our potential, intended to improve the overall effectiveness and efficiency of the franchise. This comprehensive, company-wide program is focused on generating ideas from colleagues designed to:

        - Simplify processes to better serve its customers
        - Reduce costs and grow revenue
        - Become more innovative and adapt to changing customer preferences

    - On January 7, 2014, RBSCFG announced the sale of its Chicago-area retail branches, small business operations and select middle market relationships in the Chicago market to U.S. Bank National Association, the lead bank of U.S. Bancorp (NYSE: USB). RBSCFG will maintain a presence in Chicago through its Commercial Banking and Consumer Banking divisions. The Company will continue a diverse range of commercial and consumer banking services. The sale, expected to close in mid-2014 (subject to regulatory approval), included 94 Charter One branches in the Chicago area, $5.3 billion in local deposits and $1.1 billion in locally originated loans. The proceeds will be reinvested in the remaining franchise, where the Company has stronger market positions and better long-term growth prospects.

- **Regulators:** RBS Citizens remains committed to implementing a comprehensive enterprise risk management program through enhancements across four key management areas:

  - Governance and organization
  - Values and incentives
  - Risk management processes
  - Infrastructure and resources

  The critical objectives of its enterprise risk management program are to have fully developed and embedded policies, frameworks and standards, clearly articulated roles and responsibilities across all lines of defense, and a culture that reinforces and rewards risk-based behaviors.

  RBS Citizens has made significant progress towards these objectives during 2013 including the development and syndication of a comprehensive implementation plan and the execution of key improvement initiatives.

  More specifically, the Risk Governance structure was streamlined to eliminate redundancies, clarify roles and responsibilities, and improve the identification and remediation of key and emerging risks. Targeted organizational changes were made within the Compliance and Operational Risk functions, including the build-out of a robust and independent compliance assurance function to meet the demands of a full enterprise risk management program. In addition, improvements were made to several Compliance policies and procedures, Regulatory Change Management, and Regulatory Relations.

  The creation of a long-term Enterprise Risk technology strategy has commenced with the selection of a Governance, Risk & Compliance (GRC) tool and development of an implementation roadmap.

  Incorporation of risk objectives into the performance management process has enhanced risk accountability across the organization.

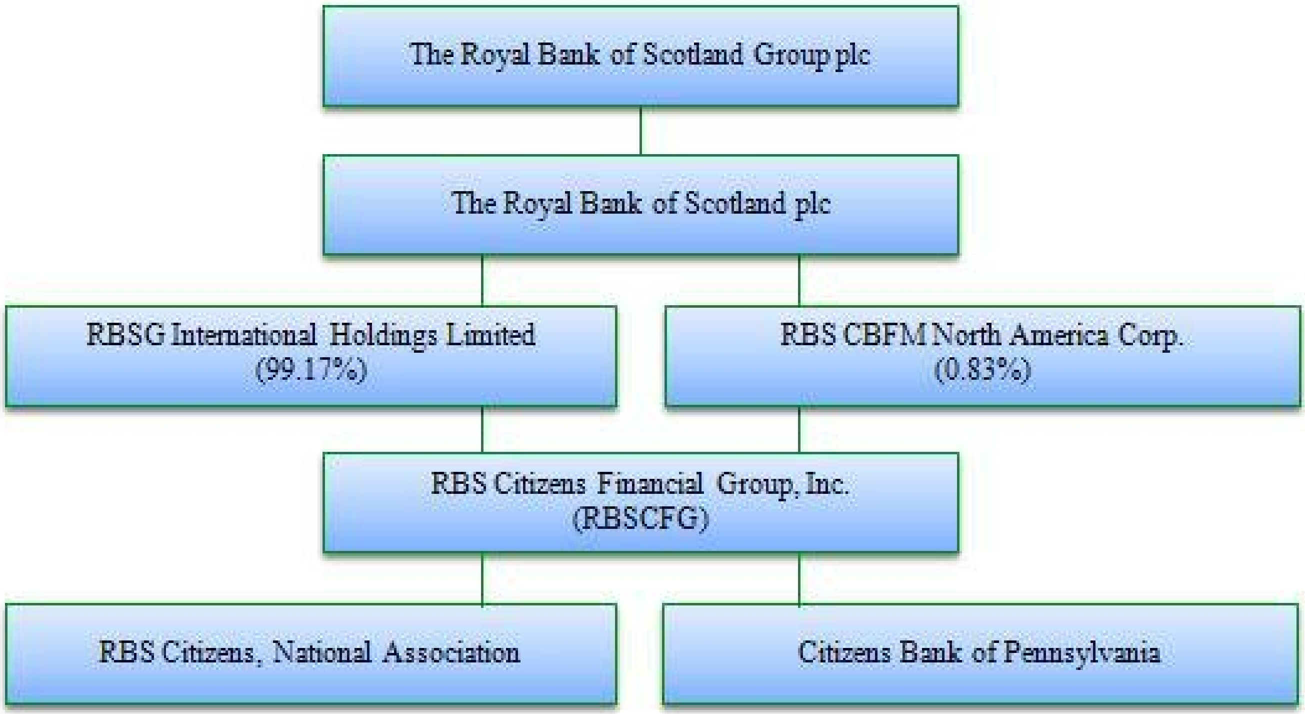
- **Colleagues:** In a rapidly evolving and challenging business environment, the Company has focused its people agenda on ensuring that managers and colleagues are highly productive, collaborative, engaged, adaptable and resilient while maintaining an unyielding commitment to customers. To that end, RBS Citizens has embarked on creating a talent management strategy that includes recruiting and selection, talent, succession, and workforce planning, leadership development, organizational structure and compensation. Results of the 2013 RBSCFG employee feedback survey demonstrate that colleagues remain highly engaged and productive in the face of change; and colleagues focus on delivering value to the customer through emphasis on understanding customer needs, being responsive and looking for better ways to serve the customer. The colleague survey also indicated that managers have excelled in leading their teams, particularly in terms of decision-making, ensuring that colleagues are applying their skills and abilities and building a strong sense of teamwork/collaboration.

- **Community:** RBS Citizens has developed a broad community strategy around the premise "When the community prospers, we all prosper; when the community is healthy and vibrant, it anchors growing families and strong businesses". RBS Citizens leverages franchise strengths to make a difference in neighborhoods across its footprint. These efforts include colleagues volunteering side-by-side with their neighbors, a foundation helping fund a range of non-profit organizations, and executives providing board leadership to community organizations. The Company also focuses its charitable giving on areas it believe will help strengthen the economic vitality within its footprint. This effort, branded "Citizens Helping Citizens" focuses on fighting hunger, providing shelter, teaching money management and strengthening communities. Colleague engagement increased during 2013 highlighted by a 27% increase in colleague volunteerism to more than 76,000 hours and an estimated value of $1.7 million. In addition, colleagues serve on more than 440 community boards across the footprint. RBS Citizens delivers on its commitment to the community through local sponsorships and signature programs including:

  - Champions in Action: a bi-annual grant competition in partnership with local media outlets to spread awareness of a local non-profit's mission.
  - Gear for Grades: a back to school backpack and supplies initiative.
  - Growing Communities: a neighborhood revitalization and economic development program for non-profits.

Our Structure

RBS Citizens is a wholly-owned subsidiary of RBS Group with two primary subsidiaries, RBS Citizens, N.A., a national banking association, and Citizens Bank of Pennsylvania, a Pennsylvania-chartered savings bank. The organizational chart below has been simplified to more clearly illustrate RBS Citizens relationship with RBS Group and its bank subsidiaries.



RBS Citizens principal business divisions, consumer banking and commercial banking, provide a wide range of retail and commercial banking products and services to consumers and businesses. Utilizing its full range of capabilities, the Company aims to provide the diversified and sophisticated products and services at the level of a national financial services institution. With a network of about 1,400 branches and a work force with close relationships with customers, RBS Citizens delivers those products and services locally with a community-oriented approach.

Consumer Banking

RBS Citizens' Consumer Banking Division focuses on retail customers and small businesses with annual revenues of less than $25 million. It offers traditional banking products and services including checking, savings, home loans, student loans, credit cards, business loans and wealth management services. The Company's multi-dimension distribution system includes a network of approximately 1,400 traditional and in-store branches, a network of more than 3,500 ATMs, call centers, online and mobile channels, and a workforce of experienced specialists ranging from financial consultants, mortgage loan officers, business banking officers and private bankers.

Commercial Banking

The Commercial Banking division targets companies with annual revenues from $25 million to $2 billion and provides a full complement of financial products and solutions including loans, leases, trade financing, deposits, cash management, foreign exchange, interest rate risk management, corporate finance and capital markets advisory capabilities. Approximately two-thirds of the revenue for the Commercial Banking Division is related to basic lending and deposit gathering for businesses. The division has dedicated teams with industry expertise in government banking, not-for-profit, healthcare, technology, asset finance, franchise finance, asset-based lending, commercial real estate, private equity and sponsor finance.

Competition

The financial services industry is highly competitive. RBS Citizens competes actively with national, regional, and local financial services providers including banks, thrifts, credit unions, mortgage brokers, investment advisory services, and other financial institutions, some of which are not subject to the same degree of regulation and restrictions imposed upon the Company. Competition among providers of financial products and services continues to intensify, with consumers having the opportunity to select from a growing variety of traditional and nontraditional alternatives. The primary factors driving consumer and commercial competition for loans and deposits are interest rates, fees, customer service levels, and the range of products and services offered. This competitive trend is likely to continue.

Employees

At December 31, 2013, RBS Citizens had approximately 19,000 employees. None of its employees are parties to a collective bargaining agreement. RBS Citizens considers its relationship with its employees to be strong.

Legal Proceedings

Contingencies

The Company operates in a legal and regulatory environment that exposes RBS Citizens to potentially significant risks. A certain amount of litigation ordinarily results from the nature of the Company's banking and other businesses. The Company is a party to legal proceedings, including class actions. It is also the subject of investigations, reviews, and regulatory matters arising out of its normal business operations, which, in some instances, relate to concerns about unfair and / or deceptive practices and mis-selling of certain products. In addition, the Company engages in discussions with relevant governmental and regulatory authorities on an ongoing and regular basis regarding various issues, and it is possible that any issues discussed or identified may result in investigatory or other action being taken. Litigation and regulatory matters may result in settlements, damages, fines, public or private censure, increased costs, required remediation, restriction on business activities, or other impact on the Company.

In these disputes and proceedings, the Company contests liability and the amount of damages as appropriate. Given their complex nature, it may be years before some of these matters are finally resolved. Moreover, before liability can be reasonably estimated for a claim, numerous legal and factual issues may need to be examined, including through potentially lengthy discovery and determination of important factual matters, and by addressing novel or unsettled legal issues relevant to the proceedings in question.

The Company cannot predict with certainty if, how, or when such claims will be resolved or what the eventual settlement, fine, penalty or other relief, if any, may be, particularly for claims that are at an early stage in their development or where claimants seek substantial or indeterminate damages. The Company recognizes a provision for a claim when, in the opinion of management after seeking legal advice, it is probable that a liability exists and the amount of loss can reasonably be estimated. In many proceedings, however, it is not possible to determine whether any loss is probable or to estimate the amount of any loss. In each of the matters described below, the Company is unable to reliably estimate the liability in excess of any provision accrued, if any, that might arise or its effects on the Company's Consolidated Statements of Operations or Consolidated Cash Flows in any particular period.

Set out below are descriptions of significant legal matters involving the Company. Based on information currently available, the advice of legal and other counsel, and established reserves, management believes that the aggregate liabilities, if any, arising from these proceedings will not have a materially adverse effect on the Company's Consolidated Financial Statements.

Fair Labor Standards Act Litigation

The Company has been named in several purported class actions brought under the FLSA and equivalent state statutes alleging that certain categories of branch employees were denied overtime for hours worked. These suits are brought by current and former branch employees alleging that either: (1) they are / were in Assistant Branch Manager positions and were improperly classified as exempt under the FLSA thereby denying them pay for all hours worked, including overtime pay; or (2) they are / were properly classified as non-exempt tellers, bankers or the like but were told not to record all of their hours, had hours they entered deleted by their managers and / or were otherwise denied pay for hours worked, including overtime pay. These cases cover the Company's entire thirteen state footprint, and they have been settled in principle, subject to court approval. Separately, the Company has been named in two lawsuits brought by current and former mortgage loan officers and home loan advisors alleging that they were improperly classified as exempt under the FLSA and corresponding state laws and therefore denied pay for all hours worked, including overtime pay. These cases have been settled, and final court approval of the settlements was granted on January 29, 2014.

Mortgage Repurchase Demands

The Company is an originator and servicer of residential mortgages and routinely sells such mortgage loans in the secondary market and to government-sponsored entities. In the context of such sales, the Company makes certain representations and warranties regarding the characteristics of the underlying loans and, as a result, may be contractually required to repurchase such loans or indemnify certain parties against losses for certain breaches of those representations and warranties. Between the start of January 2009 and the end of December 2013, the Company has received approximately $119 million in repurchase demands and $89 million in indemnification payment requests in respect of loans originated, for the most part, since 2003. Of those claims presented, $64 million was paid to repurchase residential mortgage loans, and $25 million was incurred for indemnification costs to make investors whole. The Company repurchased mortgage loans totaling $35 million and $13 million for the twelve months ended December 31, 2013 and 2012, respectively. The Company incurred indemnification costs of $12 million and $5 million for the twelve months ended December 31, 2013 and 2012, respectively. The Company cannot estimate what the future level of repurchase demands will be or the Company’s ultimate exposure, and cannot give any assurance that the historical experience will continue in the future. It is possible that the volume of repurchase demands will increase.

MERS Cases

Counties in four states are plaintiffs in suits against MERSCORP, Inc., MERS and its shareholder financial institutions, including the Company, for its origination and securitization of mortgage loans using the MERS system. The plaintiffs allege that by registering properties in MERS’ name the banks fail to pay recording fees as required by state law when properties are transferred among them. Complaints have been dismissed in two states with one such dismissal being affirmed by U.S. Court of Appeals for the Seventh Circuit and the other subject to a motion for reconsideration. The other cases continue. The Company is vigorously defending these matters.

LIBOR Litigation

The Company is a defendant in lawsuits in which allegations have been made that its parent company, RBS Group, manipulated U.S. dollar LIBOR to the detriment of the plaintiffs. The lawsuits include a purported class action on behalf of borrowers of the Company whose interest rate was tied to U.S. dollar LIBOR. The Company is vigorously defending these matters.

Foreclosure-Related Expenses

In May 2013, the civil division of the U.S. Attorney's Office for the Southern District of New York served a subpoena pursuant to the Financial Institutions Reform, Recovery and Enforcement Act of 1989 seeking information regarding home mortgage foreclosure expenses submitted for reimbursement to the United States Department of Housing and Urban Development, FNMA, or FHLMC. The Company is cooperating with the investigation.

Consumer Products

The activities of the Company’s bank subsidiaries are subject to extensive laws and regulations concerning unfair or deceptive acts or practices in connection with customer products. Certain of the bank subsidiaries’ practices with respect to overdraft protection and other consumer products have not met applicable standards. The bank subsidiaries have implemented and are continuing to implement changes to bring their practices in conformity with applicable laws and regulations. In April 2013, the bank subsidiaries consented to the issuance of orders by the OCC and the FDIC (the Consent Orders). In the Consent Orders (which are publicly available and will remain in effect until terminated by the regulators), the bank subsidiaries neither admitted nor denied the regulators’ findings that they had engaged in deceptive marketing and implementation of the bank’s overdraft protection program, checking rewards programs, and stop-payment process for pre-authorized recurring electronic fund transfers. The Consent Orders require the bank subsidiaries to pay a total of $10 million in civil monetary penalties, to develop plans to provide restitution to affected customers (the amount of which is anticipated to be approximately $8 million), to cease and desist any operations in violation of Section 5 of the Federal Trade Commission Act, and to submit to the regulators periodic written progress reports regarding compliance with the Consent Orders. In addition, RBS Citizens, N.A. agreed to take certain remedial actions to improve its compliance risk management systems and to create a comprehensive action plan designed to achieve compliance with the Consent Order. Restitution plans have been prepared and submitted for approval and RBS Citizens, N.A. has submitted for approval, and is in the process of implementing, its action plan for compliance with the Consent Order, as well as updated policies, procedures, and programs related to its compliance risk management systems.

The Company's bank subsidiaries have also identified issues regarding, among other things, certain identity theft and debt cancellation products, certain overdraft fees, the bank subsidiaries' policies and practices with respect to identifying and correcting errors in customer deposits, and the charging of cost-based credit card late payment fees. The bank subsidiaries have paid restitution, or expect to pay restitution, to certain affected customers in connection with certain of these practices. In addition, the bank subsidiaries could face formal administrative enforcement actions from their federal supervisory agencies, including the assessment of civil monetary penalties and restitution, relating to the past practices and policies identified above and other consumer products, and they could face potential civil litigation. The Company does not expect that the aggregate of amounts paid in connection with these matters will have a material adverse effect on the Company's business, financial condition and results of operations.

Relationship with RBS Group

All outstanding shares of RBS Citizens' common stock are owned by two subsidiaries of RBS Group, RBSG International Holdings Ltd and RBS CBFM North America Corp. These entities own 99.17% and 0.83%, respectively, of RBS Citizens' common stock. As a result, RBS Group can elect all of its directors and control the vote on all matters, including the following, in each case, subject to any applicable regulatory restrictions: approval of mergers or other business combinations; a sale of all or substantially all of its assets; issuance of any additional common stock or other equity securities; incurrence of debt other than in the ordinary course of business; the selection and tenure of its chief executive officer; payment of dividends with respect to its common stock or other equity securities, subject to regulatory approval; and other matters that might be favorable to RBS Group.

Nonetheless, various U.S. laws and regulations place constraints on distributions of capital, including through payment of dividends and repurchases of securities, by RBS Citizens to its parent entities, and on other intra-group transactions. These protections include: (i) the prohibitions on such distributions of capital imposed by the Federal Reserve's rules regarding submission by certain large BHCs, including RBS Citizens, of annual capital plans to the Federal Reserve (other than capital distributions made in accordance with such submitted capital plans and as to which the Federal Reserve has not objected, or otherwise in compliance with those rules); (ii) the restrictions placed by applicable U.S. federal and state laws and regulations on payment of dividends to RBS Citizens by its bank subsidiaries, on which RBS Citizens typically relies for substantially all of its revenue; and (iii) the limitations (including requirements for specified collateralization and exposure caps) on transactions between RBS Citizens' bank subsidiaries, on the one hand, and RBS Citizens and its other affiliates, on the other hand, pursuant to Sections 23A and 23B of the Federal Reserve Act and the Federal Reserve's Regulation W thereunder.

RBS Citizens conducts business in compliance with RBS Group policy standards, but also maintains comprehensive U.S. legal-entity policies and procedures aimed at ensuring compliance with local laws and regulations. The Company's operations are generally independent of the other entities within RBS Group. RBS Citizens has a $50 million revolving line of credit with RBS Group, which was not drawn upon as of December 31, 2013. RBS Citizens enters into interest rate swap and cap agreements and foreign exchange contracts with RBS Group for the purpose of reducing its exposure to fluctuations in interest rates and foreign currency exchange rates.

Subject to what the Company believes to be arm's-length commercial terms, RBS Citizens has issued a guarantee to RBS Group for a fee, whereby RBS Citizens will absorb credit losses related to the sale of option contracts by RBS Group to its customers. RBS Citizens receives income for providing services and referring customers to RBS Group and shares office space with certain RBS Group entities.