Company Number: 02263951

GOLDMAN SACHS INTERNATIONAL

(unlimited company)

ANNUAL REPORT

31 DECEMBER 2014

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Part 1: Strategic report

STRATEGIC REPORT

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

1. Introduction

Goldman Sachs International ('the company' or 'GSI') provides a wide range of financial services to clients located worldwide. The company also operates a number of branches across Europe, the Middle East and Africa ('EMEA') to provide financial services to clients in those regions.

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

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

GSI seeks to be the advisor of choice for its global clients and a leading participant in global financial markets. As part of GS Group, GSI also enters into transactions with affiliates in the normal course of business as part of market-making activities and general operations. GSI, consistent with GS Group, reports its activities in four business segments: Investment Banking; Institutional Client Services; Investing & Lending; and Investment Management.

Note on presentation

Unless otherwise stated, all amounts in this annual report are prepared in accordance with United Kingdom Generally Accepted Accounting Practice ('U.K. GAAP').

Certain disclosures required by U.K. GAAP in relation to the company's financial risk management and capital management have been presented alongside other risk management and regulatory information in the strategic report. Such disclosures are highlighted as audited. All other information in the strategic report is unaudited.

2. Financial overview

References to 'the financial statements' refer to the directors' report and audited financial statements as presented in Part 2 of this annual report for the year ended 31 December 2014. Comparative information has been presented for the year ended 31 December 2013. All references to 2014 and 2013 refer to the years ended, or the dates, as the context requires, 31 December 2014 and 31 December 2013, respectively.

GS Group prepares consolidated financial statements under United States Generally Accepted Accounting Principles ('U.S. GAAP'), which include the results of GSI prepared on a U.S. GAAP basis. The company's profit under U.K. GAAP differs to that under U.S. GAAP primarily due to timing differences in the recognition of certain revenues and expenses. The company's total assets and total liabilities under U.S. GAAP are significantly lower than those presented under U.K. GAAP, as the company is able to net a significant proportion of its derivative assets and liabilities under U.S. GAAP. Refer to *Balance sheet* below for further details.

Profit and loss account

The profit and loss account for 2014 is set out on page 61 of this annual report. Net revenue was US$5.9 billion for 2014 (2013: US$5.2 billion). The results for the company show a profit on ordinary activities before taxation of US$2.1 billion for 2014 (2013: US$298 million).

STRATEGIC REPORT (continued)

2. Financial overview (continued)

Balance sheet

The balance sheet as at 31 December 2014 is set out on page 62 of this annual report. GSI had total assets and total liabilities of US$993.0 billion and US$971.0 billion, respectively, as at 31 December 2014 (2013: total assets of US$816.4 billion and total liabilities of US$796.1 billion). The increase in total assets and total liabilities was primarily attributable to the increase in financial instruments mainly as a result of market movements during the year.

GSI had total assets and total liabilities under U.S. GAAP of US$376.3 billion and US$354.2 billion, respectively, as at 31 December 2014 (2013: total assets of US$374.5 billion and total liabilities of US$354.1 billion). GSI's total assets and total liabilities under U.K. GAAP are greater than under U.S. GAAP primarily due to certain financial assets and liabilities being offset under U.S. GAAP. Under U.K. GAAP, the company presents derivative balances as gross if they are not net settled in the normal course of business, even where it has a legally enforceable right to offset those balances. Refer to *note 1m to the financial statements* for further details.

Cash flows

As a financial institution, the company's cash flows are complex and bear little relation to the company's profitability and net assets. Consequently, traditional cash flow analysis is less meaningful in evaluating the company's liquidity position than liquidity and asset-liability management policies, which are described in *Item 10 (Liquidity risk management).* Cash flow analysis may, however, be helpful in highlighting certain macro trends and strategic initiatives in the company's businesses. The statement of cash flow for 2014 is set out on page 63 of this annual report. GSI's cash decreased by US$235 million in 2014 (2013: increase of US$905 million).

Future outlook

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

3. Business environment

Global

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

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

STRATEGIC REPORT (continued)

3. Business environment (continued)

Europe

In the Euro area, real GDP increased by 0.9% in 2014, compared with a contraction of 0.4% in 2013. While an improvement from 2013, growth remained at a suppressed level. Fixed investment and consumer spending both grew modestly in 2014, after contracting in 2013, and measures of inflation remain subdued. The ECB cut the main refinancing operations and deposit rates by 20 basis points to 0.05% and (0.20)%, respectively, announced a purchase programme for asset-backed securities and covered bonds in the fourth quarter of 2014, and discussed the possibility of a quantitative easing programme targeting sovereign bonds. The Euro depreciated by 12% against the U.S. dollar. In the United Kingdom, real GDP increased by 2.6% in 2014, compared with an increase of 1.7% in 2013. The Bank of England maintained its official bank rate at 0.50%. The British pound depreciated by 6% against the U.S. dollar. Yields on 10-year government bonds in the region generally fell during the year. In equity markets, the DAX Index and the Euro Stoxx 50 Index increased by 3% and 1%, respectively, while the FTSE 100 Index and the CAC 40 Index decreased by 3% and 1%, respectively, during 2014. Tensions related to the political situation in Ukraine and Russia generated concern during the year. The U.S. dollar appreciated by 76% against the Russian ruble and, in equity markets, the MICEX Index decreased by 7% during 2014.

4. Critical accounting policy

Fair value

Fair value hierarchy. Financial instruments owned and financial instruments sold, but not yet purchased (i.e. inventory), as well as certain other financial assets and financial liabilities, are reflected in the balance sheet at fair value (i.e. marked-to-market), with related gains or losses recognised in the profit and loss account. The use of fair value to measure financial instruments is fundamental to the company's risk management practices and is the company's most critical accounting policy.

The fair value of a financial instrument is the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Certain financial assets and financial liabilities are measured as a portfolio (i.e. based on its net exposure to market and / or credit risks). In determining fair value, the hierarchy under U.K. GAAP gives (i) the highest priority to unadjusted quoted prices in active markets for identical, unrestricted assets or liabilities (level 1 inputs), (ii) the next priority to inputs other than level 1 inputs that are observable, either directly or indirectly (level 2 inputs), and (iii) the lowest priority to inputs that cannot be observed in market activity (level 3 inputs). Assets and liabilities are classified in their entirety based on the lowest level of input that is significant to their fair value measurement.

The fair values for substantially all of the company's financial assets and financial liabilities are based on observable prices and inputs and are classified in levels 1 and 2 of the fair value hierarchy. Certain level 2 and level 3 financial assets and financial liabilities may require appropriate valuation adjustments that a market participant would require to arrive at fair value for factors such as counterparty and GS Group's credit quality, funding risk, transfer restrictions, liquidity and bid / offer spreads. Valuation adjustments are generally based on market evidence. Instruments categorised within level 3 of the fair value hierarchy are those which require one or more significant inputs that are not observable. As at 31 December 2014, the company had level 3 financial assets under U.K. GAAP of US$15.2 billion (2013: US$13.6 billion). As at 31 December 2014, the company had level 3 financial assets under U.S. GAAP of US$9.2 billion (2013: US$8.0 billion). Absent evidence to the contrary, instruments classified within level 3 of the fair value hierarchy are initially valued at transaction price, which is considered to be the best initial estimate of fair value. Subsequent to the transaction date, other methodologies are used to determine fair value, which vary based on the type of instrument. Estimating the fair value of level 3 financial instruments requires judgements to be made. These judgements include:

- Determining the appropriate valuation methodology and / or model for each type of level 3 financial instrument;

- Determining model inputs based on an evaluation of all relevant empirical market data, including prices evidenced by market transactions, interest rates, credit spreads, volatilities and correlations; and

- Determining appropriate valuation adjustments, including those related to illiquidity or counterparty credit quality.

STRATEGIC REPORT (continued)

4. Critical accounting policy (continued)

Regardless of the methodology, valuation inputs and assumptions are only changed when corroborated by substantive evidence.

Controls over valuation of financial instruments. Market makers and investment professionals in the company's revenue-producing units are responsible for pricing financial instruments. The company's control infrastructure is independent of the revenue-producing units and is fundamental to ensuring that all financial instruments are appropriately valued at market-clearing levels. In the event that there is a difference of opinion in situations where estimating the fair value of financial instruments requires judgement (e.g. calibration to market comparables or trade comparison, as described below), the final valuation decision is made by senior managers in control and support functions that are independent of the revenue-producing units. This independent price verification is critical to ensuring that the company's financial instruments are properly valued.

Price verification. All financial instruments at fair value in levels 1, 2 and 3 of the fair value hierarchy are subject to the company's independent price verification process. The objective of price verification is to have an informed and independent opinion with regard to the valuation of financial instruments under review. Instruments that have one or more significant inputs which cannot be corroborated by external market data are classified within level 3 of the fair value hierarchy. Price verification strategies utilised by independent control and support functions include:

- Trade comparison: analysis of trade data (both internal and external where available) is used to determine the most relevant pricing inputs and valuations.

- External price comparison: valuations and prices are compared to pricing data obtained from third parties (e.g. broker or dealers, MarkIt, Bloomberg). Data obtained from various sources is compared to ensure consistency and validity. When broker or dealer quotations or third-party pricing vendors are used for valuation or price verification, greater priority is generally given to executable quotations.

- Calibration to market comparables: market-based transactions are used to corroborate the valuation of positions with similar characteristics, risks and components.

- Relative value analyses: market-based transactions are analysed to determine the similarity, measured in terms of risk, liquidity and return, of one instrument relative to another or, for a given instrument, of one maturity relative to another.

- Collateral analyses: margin calls on derivatives are analysed to determine implied values which are used to corroborate valuations.

- Execution of trades: where appropriate, trading desks are instructed to execute trades in order to provide evidence of market-clearing levels.

- Backtesting: valuations are corroborated by comparison to values realised upon sales.

Review of net revenue. Independent control and support functions ensure adherence to the company's pricing policy through a combination of daily procedures, including the explanation and attribution of net revenues based on the underlying factors. Through this process the company independently validates net revenue, identifies and resolves potential fair value or trade booking issues on a timely basis and seeks to ensure that risks are being properly categorised and quantified.

STRATEGIC REPORT (continued)

4. Critical accounting policy (continued)

Review of valuation models. GS Group's independent model validation group, consisting of quantitative professionals who are separate from model developers, performs an independent model approval process. This process incorporates a review of a diverse set of model and trade parameters across a broad range of values (including extreme and / or improbable conditions) in order to critically evaluate:

- The model's suitability for valuation and risk management of a particular instrument type;
- The model's accuracy in reflecting the characteristics of the related product and its significant risks;
- The suitability of the calculation techniques incorporated in the model;
- The model's consistency with models for similar products; and
- The model's sensitivity to input parameters and assumptions.

New or changed models are reviewed and approved prior to being put into use. Models are evaluated and re-approved annually to assess the impact of any changes in the product or market and any market developments in pricing theories.

5. Results of operations

The composition of net revenue has varied over time as financial markets and the scope of the company's operations have changed. The composition of net revenue can also vary over the short-term due to fluctuations in economic and market conditions. In addition to transactions entered into with third parties, the company also enters into transactions with affiliates in the normal course of business as part of market-making activities and general operations. Refer to *note 3 to the financial statements* for further details.

Net revenue

Net revenue includes the net profit arising from transactions, with both affiliates and third parties, in securities, foreign exchange and other financial instruments, and fees and commissions. This is inclusive of expenses related to market-making activities (i.e. brokerage, clearing, exchange and distribution fees), and associated interest and dividends. Refer to *note 3 to the financial statements* for further details.

For 2014, net revenue was US$5.9 billion (2013: US$5.2 billion). The increase of US$742 million reflected significantly higher net revenues in Investment Banking and Investing & Lending and, to a lesser extent, Investment Management. Net revenues in Institutional Client Services were essentially unchanged.

Refer to *Segment reporting* below for further details.

Administrative expenses

Administrative expenses are primarily influenced by compensation (including the impact of the Group Inc. share price on share-based compensation), headcount and levels of business activity. Administrative expenses were US$3.6 billion for 2014, 20% lower than 2013 (2013: US$4.5 billion). The decrease was primarily due to the impact of the mark-to-market of share-based compensation.

Direct costs of employment include salaries, allowances, discretionary compensation, amortisation and mark-to-market of share-based compensation and other items such as benefits. Discretionary compensation is significantly impacted by, among other factors, the level of net revenues, overall financial performance, prevailing labour markets, business mix, the structure of share-based compensation programmes and the external environment.

STRATEGIC REPORT (continued)

5. Results of operations (continued)

Direct costs of employment were US$3.0 billion for 2014, 20% lower than 2013 (2013: US$3.8 billion). The mark-to-market of share-based compensation awarded in prior years by Group Inc. was a charge of US$83 million due to an appreciation of the Group Inc. share price in 2014 (2013: charge of US$1.0 billion). Excluding the impact of the mark-to-market of share-based compensation, direct costs of employment were US$3.0 billion for 2014, 6% higher than the prior year (2013: US$2.8 billion). The average number of the company's staff (employees including directors, and consultants and temporary staff) was 5,582 in 2014, 2% higher than in 2013.

Administrative expenses excluding direct costs of employment were US$582 million (2013: US$738 million). The decrease was primarily due to lower miscellaneous taxes and higher management recharges to affiliates.

Interest payable and similar charges

Interest payable and similar charges comprises interest on long-term subordinated loans from group undertakings of US$222 million for 2014 (2013: US$306 million). The decrease was due to a reduction in the average long-term subordinated loans balance in comparison to 2013.

Tax on profit on ordinary activities

Tax on profit on ordinary activities was US$456 million for 2014 (2013: US$129 million). This increase was mainly due to an increase in profit on ordinary activities before taxation. The effective tax rate for 2014 was 21.9%, down from 43.3% for 2013. The decrease in the effective tax rate was primarily due to non-recurring deferred tax write-downs in 2013 and a reduction in the U.K. corporation tax rate to 21.5% in 2014 (2013: 23.25%).

Segment reporting

The company's net revenue is categorised into the following business segments:

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Investment Banking		
Financial Advisory	444,352	342,960
Underwriting	935,329	754,971
	1,379,681	**1,097,931**
Institutional Client Services		
Fixed Income, Currency and Commodities Client Execution	2,187,273	2,198,951
Equities	1,575,155	1,516,429
	3,762,428	**3,715,380**
Investing & Lending[1]	**266,853**	**14,740**
Investment Management[1]	**489,640**	**328,637**
Net revenue	**5,898,602**	**5,156,688**

1. The company has reclassified US$150 million of net revenue for 2013 from Investing & Lending to Investment Management associated with providing investing services to funds managed by GS Group. There is no impact to total net revenue.

STRATEGIC REPORT (continued)

5. Results of operations (continued)

Investment Banking

Investment Banking is comprised of:

Financial Advisory. Includes strategic advisory engagements with respect to mergers and acquisitions, divestitures, corporate defence activities, restructurings, spin-offs, risk management and derivative transactions directly related to these client advisory engagements.

Underwriting. Includes equity and debt underwriting of public offerings and private placements across a wide range of securities and other financial instruments, and derivative transactions directly related to these client underwriting activities.

2014 versus 2013. Net revenues in Investment Banking were US$1.4 billion, 26% higher than 2013. Net revenues in Underwriting were US$935 million, 24% higher than 2013, primarily due to significantly higher net revenues in equity underwriting, principally from initial public offerings, and higher net revenues in debt underwriting, principally from high-yield related activity. Net revenues in Financial Advisory were significantly higher compared with 2013, reflecting an increase in industry-wide completed mergers and acquisitions.

During 2014, Investment Banking operated in an environment generally characterised by strong industry-wide underwriting activity in both equity and debt, and an increase in industry-wide completed mergers and acquisitions activity compared with 2013. Industry-wide announced mergers and acquisitions activity significantly increased compared with 2013.

At the end of 2014, the company's investment banking transaction backlog increased compared to the end of 2013, due to a significant increase in estimated net revenues from potential advisory transactions, and an increase in estimated net revenues from potential underwriting transactions. The latter represented an increase in estimated net revenues from potential leveraged finance underwriting transactions offset by a significant decrease in estimated net revenues from potential equity underwriting transactions, particularly in initial public offerings.

The company's investment banking transaction backlog represents an estimate of future net revenues from investment banking transactions where the company believes that future revenue realisation is more likely than not. The company believes changes in its investment banking transaction backlog may be a useful indicator of client activity levels which, over the long term, impact net revenues. However, the time frame for completion and corresponding revenue recognition of transactions in the backlog varies based on the nature of the engagement, as certain transactions may remain in the backlog for longer periods of time and others may enter and leave within the same reporting period. In addition, the company's transaction backlog is subject to certain limitations, such as assumptions about the likelihood that individual client transactions will occur in the future. Transactions may be cancelled or modified, and transactions not included in the estimate may also occur.

Institutional Client Services

Institutional Client Services generates revenues in three ways:

- In large, highly liquid markets, the company executes a high volume of transactions for clients for modest spreads and fees;
- In less liquid markets, the company executes transactions for clients for spreads and fees that are generally somewhat larger; and
- The company also structures and executes transactions involving customised or tailor-made products that address clients' risk exposures, investment objectives or other complex needs.

STRATEGIC REPORT (continued)

5. Results of operations (continued)

Institutional Client Services is comprised of:

Fixed Income, Currency and Commodities Client Execution. Includes client execution activities related to making markets in interest rate products, credit products, mortgages, currencies and commodities.

- **Interest rate products.** Government bonds, money market instruments such as commercial paper, treasury bills, repurchase agreements and other highly liquid securities and instruments, as well as interest rate swaps, options and other derivatives.

- **Credit products.** Investment-grade corporate securities, high-yield securities, credit derivatives, bank and bridge loans, municipal securities, emerging market and distressed debt, and trade claims.

- **Mortgages.** Commercial mortgage-related securities, loans and derivatives, residential mortgage-related securities, loans and derivatives, and other asset-backed securities, loans and derivatives.

- **Currencies.** Most currencies, including growth-market currencies.

- **Commodities.** Crude oil and petroleum products, natural gas, base, precious and other metals, electricity, coal, agricultural and other commodity products.

Equities. Includes client execution activities related to making markets in equity products and commissions and fees from executing and clearing institutional client transactions on major stock, options and futures exchanges worldwide, as well as over-the-counter ('OTC') transactions. Equities also includes the securities services business, which provides financing, securities lending and other prime brokerage services to institutional clients, including hedge funds, mutual funds, pension funds and foundations, and generates revenues primarily in the form of interest rate spreads or fees.

2014 versus 2013. Net revenues in Institutional Client Services were US$3.8 billion, essentially unchanged in comparison to 2013.

Net revenues in Fixed Income, Currency and Commodities Client Execution were US$2.2 billion, essentially unchanged compared with 2013, as significantly lower net revenues in credit products and mortgages and lower net revenues in currencies were partially offset by significantly higher net revenues in interest rate products.

Net revenues in Equities were US$1.6 billion, 4% higher than 2013, due to higher net revenues in securities services and commissions and fees. This was partially offset by lower net revenues in equities client execution.

During 2014, Institutional Client Services continued to operate in a challenging environment, as economic uncertainty contributed to subdued risk appetite for clients and generally low levels of activity. In addition, volatility levels remained low, although volatility and activity levels increased in certain businesses towards the end of the year. Debt markets were also impacted by the widening of high-yield credit spreads and the decline in oil prices during the second half of the year, which contributed to low liquidity, particularly in credit. Equity markets, however, generally increased during the year.

Investing & Lending

Investing & Lending includes direct investments made by the company, which are typically longer-term in nature.

2014 versus 2013. Net revenues in Investing & Lending were US$267 million for 2014, compared with US$15 million for 2013. 2014 net revenues were significantly higher compared with 2013 due to an increase in net gains from investments in equities, primarily driven by company-specific events.

STRATEGIC REPORT (continued)

5. Results of operations (continued)

Investment Management

Investment Management offers investment management and wealth advisory services, including portfolio management and financial counselling, and brokerage and other transaction services to high-net-worth individuals and families. Investment Management also includes net revenues associated with providing investing services to funds managed by GS Group.

2014 versus 2013. Net revenues in Investment Management were US$490 million, 49% higher than 2013, reflecting significantly higher management and other fees, primarily due to an increase in net revenues from providing investing services to funds managed by GS Group and higher average assets under supervision. In addition, net revenues from transaction services were significantly higher compared with 2013.

6. Balance sheet and funding sources

Balance sheet management

One of the most important risk management disciplines for a financial institution is its ability to manage the size and composition of its balance sheet. GSI leverages the firmwide balance sheet management process performed at the GS Group level to manage these factors. While the asset base of Group Inc. and its affiliates vary due to client activity, market fluctuations and business opportunities, the size and composition of the balance sheet reflects (i) the overall risk tolerance of GS Group, (ii) the ability to access stable funding sources and (iii) the amount of equity capital held by GS Group.

In order to ensure appropriate risk management, GSI seeks to maintain a liquid balance sheet and leverages GS Group's processes to dynamically manage assets and liabilities which include (i) quarterly planning, (ii) business-specific limits, (iii) monitoring of key metrics, and (iv) scenario analyses.

Quarterly planning. GS Group prepares a quarterly balance sheet plan that combines projected total assets and composition of assets with expected funding sources for the upcoming quarter. The objectives of this quarterly planning process are:

- To develop near-term balance sheet projections, taking into account the general state of the financial markets and expected business activity levels, as well as current regulatory requirements;

- To determine the target amount, tenor and type of funding to raise, based on projected assets and forecasted maturities; and

- To allow business risk managers and managers from independent control and support functions to objectively evaluate balance sheet limit requests from business managers in the context of overall balance sheet constraints, including GS Group's liability profile and equity capital levels, and key metrics. Limits are typically set at levels that will be periodically exceeded, rather than at levels which reflect maximum risk appetite.

The consolidated quarterly plan, including balance sheet plans by business, funding and capital projections, and projected capital and liquidity metrics, is reviewed by GS Group's Firmwide Finance Committee, a sub-committee of GS Group's Firmwide Risk Committee. Refer to *Item 9 (Overview and structure of risk management)* for an overview of GS Group and the company's risk management structure.

Business-specific limits. GS Group's Firmwide Finance Committee sets asset and liability limits for each business and aged inventory limits for certain financial instruments as a disincentive to hold inventory over longer periods of time. These limits are set at levels which are close to actual operating levels in order to ensure prompt escalation and discussion among business managers and managers in independent control and support functions on a routine basis. GS Group's Firmwide Finance Committee reviews and approves balance sheet limits on a quarterly basis and may also approve changes in limits on an *ad hoc* basis in response to changing business needs or market conditions.

STRATEGIC REPORT (continued)

6. Balance sheet and funding sources (continued)

Requests for changes in limits are evaluated after giving consideration to their impact on key GS Group metrics. Compliance with limits is monitored on a daily basis by business risk managers, as well as managers in independent control and support functions.

Monitoring of key metrics. Key balance sheet metrics are monitored daily both by business and on a consolidated basis, including asset and liability size and composition, aged inventory, limit utilisation, risk measures and capital usage. Assets are allocated to businesses and movements resulting from new business activity as well as market fluctuations are reviewed and analysed.

Scenario analyses. GS Group conducts scenario analyses for Group Inc. and its subsidiaries to determine how it would manage the size and composition of the balance sheet and maintain appropriate funding, liquidity and capital positions in a variety of situations. These scenarios cover short-term and long-term time horizons using various macroeconomic and GS Group-specific assumptions, based on a range of economic scenarios. These analyses are used to assist in developing longer-term balance sheet management strategy, including the level and composition of assets, funding and equity capital. Additionally, these analyses help in the development of approaches for maintaining appropriate funding, liquidity and capital across a variety of situations, including a severely stressed environment.

Liquidity and cash

The company maintains substantial liquidity to meet a broad range of potential cash outflows and collateral needs in the event of a stressed environment. The company's liquidity exceeds the minimum liquidity requirement as defined by the PRA's Individual Liquidity Guidance ('ILG') framework. Refer to *Item 10 (Liquidity risk management – Liquidity)* for details on the composition and sizing of the company's Global Core Liquidity Assets ('GCLA'), previously Global Core Excess ('GCE').

Funding sources

The company's primary sources of funding are secured financings, intercompany unsecured borrowings and external unsecured borrowings.

GSI raises this funding through a number of different products, including:

- Collateralised financing, which are securities sold under agreements to repurchase ('repurchase agreements') and securities loaned;
- Intercompany unsecured loans from Group Inc. and other affiliates; and
- Debt securities issued to both external counterparties and affiliates, which includes securitised derivative products (including certificates and warrants), notes and vanilla debt, as well as transfers of assets accounted for as financings rather than sales.

GSI generally distributes funding products through its own sales force and third-party distributors, to a large, diverse creditor base in a variety of global markets. The company believes that its relationships with creditors are critical to its liquidity. Creditors include banks, securities lenders, pension funds, insurance companies, mutual funds and individuals. GSI has imposed various internal guidelines to monitor creditor concentration across its external funding programmes.

STRATEGIC REPORT (continued)

6. Balance sheet and funding sources (continued)

Secured funding. The company funds a significant amount of inventory on a secured basis with external counterparties as well as with affiliates. As at 31 December 2014, secured funding with external counterparties totalled US$55.8 billion (2013: US$97.0 billion) and secured funding with affiliates totalled US$107.0 billion (2013: US$102.0 billion). Secured funding is less sensitive to changes in Group Inc. and / or GSI credit quality than unsecured funding, due to posting of collateral to lenders. Nonetheless, GSI continually analyses the refinancing risk of its secured funding activities, taking into account trade tenors, maturity profiles, counterparty concentrations, collateral eligibility and counterparty rollover probabilities. GSI seeks to mitigate its refinancing risk by executing term trades with staggered maturities, diversifying counterparties, raising excess secured funding, and pre-funding residual risk through the GCLA.

GSI seeks to raise secured funding with a term appropriate for the liquidity of the assets that are being financed, and seeks longer maturities for secured funding collateralised by asset classes that may be harder to fund on a secured basis especially during times of market stress. Assets that may be harder to fund on a secured basis during times of market stress include certain financial instruments in the following categories: mortgage and other asset-backed loans and securities; non-investment grade corporate debt securities; equities and convertible debentures; and emerging market securities. Substantially all of GSI's external secured funding, excluding funding collateralised by liquid government obligations, is executed for tenors of one month or greater.

A majority of the company's secured funding for securities not eligible for inclusion in the GCLA is executed through term repurchase agreements and securities lending contracts. The company also raises financing through other types of secured funding, such as secured loans and notes. The table below presents GSI's secured funding.

	31 December 2014 US$m	31 December 2013 US$m
Repurchase agreements	62,396	104,990
Securities loaned	94,973	85,221
Debt securities issued	2,602	6,724
Short-term secured funding	**159,971**	**196,935**
Debt securities issued	2,840	2,050
Long-term secured funding	**2,840**	**2,050**
Total	**162,811**	**198,985**

Repurchase agreements decreased US$42.6 billion to US$62.4 billion as at 31 December 2014, reflecting a firmwide reduction in client and firm financing activity, primarily resulting from a GS Group initiative to reduce activities with lower returns.

The weighted average maturity of the company's external secured funding, excluding funding collateralised by highly liquid securities eligible for inclusion in the GCLA, exceeded 120 days as at 31 December 2014.

STRATEGIC REPORT (continued)

6. Balance sheet and funding sources (continued)

Intercompany unsecured borrowings. GSI sources funding through unsecured intercompany borrowings from Group Inc. and other affiliates. The majority of GS Group's unsecured funding is raised by Group Inc., which lends the necessary funds to its subsidiaries, including GSI, to meet asset financing, liquidity and capital requirements. The benefits of this approach to subsidiary funding are enhanced control and greater flexibility to meet the funding requirements of GSI and other subsidiaries. Intercompany unsecured borrowings also include debt securities issued. The table below presents GSI's intercompany unsecured borrowings.

	31 December 2014 US$m	31 December 2013 US$m
Amounts due to parent and group undertakings	49,464	37,857
Debt securities issued	3,807	3,820
Short-term intercompany unsecured borrowings	**53,271**	**41,677**
Long-term subordinated loans	6,458	6,458
Amounts due to parent and group undertakings	2,702	3,550
Debt securities issued	471	101
Long-term intercompany unsecured borrowings	**9,631**	**10,109**
Total	**62,902**	**51,786**

Short-term amounts due to parent and group undertakings increased US$11.6 billion to US$49.5 billion as at 31 December 2014, primarily as a result of the company's increase in GCLA requirements. Refer to *Item 10 (Liquidity risk management – Liquidity)* for further details.

External unsecured borrowings. External unsecured borrowings include debt securities issued and bank loans and overdrafts. The table below presents GSI's external unsecured borrowings.

	31 December 2014 US$m	31 December 2013 US$m
Bank loans	111	43
Overdrafts	9	28
Debt securities issued	9,135	8,417
Short-term external unsecured borrowings	**9,255**	**8,488**
Debt securities issued	3,076	2,054
Long-term external unsecured borrowings	**3,076**	**2,054**
Total	**12,331**	**10,542**

Total shareholder's funds

As at 31 December 2014, GSI held US$22.0 billion (2013: US$20.3 billion) of total shareholder's funds. Refer to *Item 7 (Regulatory – Regulatory capital)* for further information on GSI's capital.

STRATEGIC REPORT (continued)

7. Regulatory

Capital management (audited)

Capital adequacy is of critical importance to the company. The company's objective is to be prudently capitalised in terms of the amount and composition of its equity base, both relative to the company's risk exposures and compared to external requirements and benchmarks. Accordingly, a comprehensive capital management policy is in place that provides a framework and a set of guidelines to assist in determining the level and composition of capital that is targeted and maintained.

The appropriate level and composition of equity capital is determined by considering multiple factors, including: current and future regulatory capital requirements; the results of the company's capital planning and stress testing process; and other factors such as rating agency guidelines, the business environment, conditions in the financial markets and assessments of potential future losses due to adverse changes in the company's business and market environments.

The company's capital planning and stress testing process incorporates internally designed stress tests and those required under the PRA's Internal Capital Adequacy Assessment Process ('ICAAP'). It is also designed to identify and measure material risks associated with business activities, including market risk, credit risk, operational risk and other risks. The company's goal is to hold sufficient capital to ensure that it remains adequately capitalised after experiencing a severe stress event. The company's assessment of capital adequacy is viewed in tandem with its assessment of liquidity adequacy and is integrated into its overall risk management structure, governance and policy framework.

In addition, as part of the company's comprehensive capital management policy, a contingency capital plan is maintained that provides a framework for analysing and responding to an actual or perceived capital shortfall, including, but not limited to, identification of drivers of a capital deficiency, as well as mitigants and potential actions. It outlines the appropriate communication procedures to follow during a crisis period, including internal dissemination of information as well as ensuring timely communication with external stakeholders.

Resolution and recovery planning

GS Group is required by the Federal Reserve Board and the Federal Deposit Insurance Corporation ('FDIC') to submit an annual plan that describes the strategy for a rapid and orderly resolution in the event of material financial distress or failure ('resolution plan'). GSI is considered to be a material entity for the purposes of the annual resolution plan prepared by GS Group. GSI submitted the 2014 resolution plan to the PRA in July 2014. In August 2014, the Federal Reserve Board and the FDIC indicated that GS Group and other large industry participants had certain shortcomings in the 2013 resolution plans that must be addressed in the 2015 resolution plans, which are required to be submitted on or before 1 July 2015.

GS Group also prepares, on an annual basis, a global recovery plan that outlines the steps that management could take to reduce risk, maintain sufficient liquidity, and conserve capital in times of prolonged stress.

The European Union ('EU') Bank Recovery and Resolution Directive ('BRRD') was published in the Official Journal of the European Union on 12 June 2014 and establishes a framework for the recovery and resolution of credit institutions and investment firms in the EU region. The BRRD was implemented in the UK on 1 January 2015, with the exception of certain powers which will come into effect by 1 January 2016. The BRRD aims to provide national supervisory authorities with tools and powers to pre-emptively address potential financial crises in order to promote financial stability and minimise taxpayers' exposure to losses.

Under the BRRD, a resolution authority is empowered to employ one or more resolution tools in relation to certain institutions, including investment firms (such as GSI), where the authority determines that the institution is failing or likely to fail, it is not reasonably likely that any other action can be taken to avoid the failure of the institution, and the resolution action is in the public interest.

STRATEGIC REPORT (continued)

7. Regulatory (continued)

The tools available to the resolution authority under the BRRD include a statutory 'write-down and conversion power,' the so-called 'bail-in' tool. The 'bail-in' tool gives the resolution authority the ability to cancel all or a portion of the principal amount of, or interest on, certain unsecured liabilities of a failing institution and to convert certain debt claims into another security, including ordinary shares of the surviving entity or bridge institution, if any.

Regulatory capital (audited)

As at 31 December 2013, the company was subject to the risk-based capital regulations of the PRA that were based on the third EU Capital Requirements Directive ('CRD III'), which in turn are based on the Basel Committee on Banking Supervision's ('Basel Committee') June 2006 framework ('Basel II'), as modified by the Basel Committee's February 2011 revisions to the market risk framework ('prior capital rules').

As of 1 January 2014, the company became subject to a revised capital framework for EU-regulated financial institutions (the fourth EU Capital Requirements Directive and EU Capital Requirements Regulation, collectively known as 'CRD IV'). These regulations are largely based on the Basel Committee's final capital framework for strengthening international capital standards ('Basel III').

The table below presents the minimum ratios currently applicable under CRD IV and the minimum ratios that the company expects will apply at the end of the transitional provisions from 1 January 2019.

	31 December 2014 Minimum ratio[1]	1 January 2015 Minimum ratio[1]	1 January 2019 Minimum ratio[2]
Common Equity Tier 1 ('CET1') ratio	4.0%	4.5%	7.0%
Tier 1 capital ratio	5.5%	6.0%	8.5%
Total capital ratio	8.0%	8.0%	10.5%

1. Does not reflect the capital conservation buffer or potential Domestic Systemically Important Banks buffer.
2. The minimum ratios from 1 January 2019 include the required increases on 1 January 2015 and the capital conservation buffer of 2.5%.

The CET1 ratio is defined as CET1 divided by risk-weighted assets ('RWAs'). The Tier 1 capital ratio is defined as Tier 1 capital divided by RWAs. The total capital ratio is defined as total capital divided by RWAs.

Under CRD IV, on 1 January 2015, the minimum CET1 ratio increased from 4.0% to 4.5% and the minimum Tier 1 capital ratio increased from 5.5% to 6.0%. In addition, these minimum ratios will be supplemented by a new capital conservation buffer, consisting entirely of capital that qualifies as CET1, that phases in, beginning 1 January 2016, in increments of 0.625% per year until it reaches 2.5% of RWAs on 1 January 2019. GSI's future capital requirements may also be impacted by developments such as the introduction of additional capital buffers.

GSI was in compliance with external capital requirements as at 31 December 2014 and 31 December 2013.

Regulatory capital ratios

The table below presents a breakdown of GSI's capital ratios under CRD IV on a fully phased-in basis as at 31 December 2014. The prior year estimated capital ratios have been prepared under the assumption that the CRD IV rules, applicable since 1 January 2014, applied as at 31 December 2013.

	31 December 2014	31 December 2013
CET1 ratio	9.7%	8.7%
Total capital ratio	12.7%	11.6%

STRATEGIC REPORT (continued)

7. Regulatory (continued)

As at 31 December 2014 and 31 December 2013, GSI did not have any financial instruments which qualified as additional Tier 1 capital and the Tier 1 capital ratio was identical to the CET1 ratio disclosed above.

Although the fully phased-in capital ratios under CRD IV are not applicable until 2019, they are meaningful because they are measures that the company and its regulators and investors use to assess the company's ability to meet future regulatory capital requirements.

Certain CRD IV rules are subject to final technical standards and clarifications, which will be issued by the European Banking Authority ('EBA') and adopted by the European Commission and PRA. All capital, RWAs and estimated ratios are based on current interpretation, expectations and understanding of CRD IV and may evolve as its interpretation and application is discussed with the company's regulators.

As at 31 December 2013, GSI had a Tier 1 capital ratio of 14.4% and a total capital ratio of 18.5% under CRD III. These ratios were calculated under the prior capital rules and are not comparable to the company's capital ratios under CRD IV, presented in the table above.

Capital resources (audited)

The table below presents a breakdown of GSI's capital components under CRD IV on a fully phased-in basis as at 31 December 2014. The 2013 estimated capital components have been prepared under the assumption that the CRD IV rules, applicable since 1 January 2014, applied as at 31 December 2013.

	31 December 2014 US$m	31 December 2013 US$m
Called up share capital	533	533
Share premium account including capital reserves	2,880	2,880
Audited retained earnings	18,584	16,887
CET1 (before deductions)	21,997	20,300
Deductions from CET1	(906)	(568)
CET1	**21,091**	**19,732**
Tier 2 capital (long-term subordinated loans)	**6,458**	**6,458**
Total capital resources (net of deductions)	**27,549**	**26,190**

Risk-weighted assets

The table below presents the components of RWAs within GSI's regulatory capital ratios under CRD IV as at 31 December 2014. The 2013 estimated components of RWAs have been prepared under the assumption that the CRD IV rules, applicable since 1 January 2014, applied as at 31 December 2013.

RWAs	31 December 2014 US$m	31 December 2013 US$m
Credit RWAs	127,346	127,488
Concentration RWAs	2,114	-
Market RWAs	75,958	85,000
Operational RWAs	11,804	13,500
Total RWAs	**217,222**	**225,988**

STRATEGIC REPORT (continued)

7. Regulatory (continued)

Credit risk

Credit RWAs are calculated based upon measures of exposure, which are then risk weighted. The exposure amount is generally based on the following:

- For on-balance-sheet assets, the carrying value; and

- For off-balance-sheet exposures, including commitments and guarantees, a credit equivalent exposure amount is calculated based on the notional amount of each exposure multiplied by a credit conversion factor.

Counterparty credit risk is a component of total credit risk, and includes credit exposure arising from derivatives, securities financing transactions and margin loans.

GSI has been approved by the PRA to use the Internal Models Methodology for the measurement of exposure on derivatives, securities financing transactions and margin loans. For substantially all of the counterparty credit risk arising from these products, internal models are used to calculate the exposure at default ('EAD'), which is an estimate of the amount that would be owed to the company at the time of a default. The EAD takes into account the impact of netting and collateral, however does not include the effect of any economic hedges.

All exposures are then assigned a risk weight. GSI has been approved by the PRA to compute risk weights for certain exposures in accordance with the Advanced Internal Ratings-Based ('AIRB') approach, which utilises internal assessments of each counterparty's creditworthiness.

RWAs are calculated by multiplying EAD by the counterparty's risk weight. Under the CRD IV AIRB approach, a counterparty's risk weight is a function of its probability of default ('PD'), loss given default ('LGD') and the effective maturity of the trade or portfolio of trades, where:

- PD is an estimate of the probability that an obligor will default over a one-year horizon – PD is derived from the use of internally determined equivalents of external credit assessment ratings; and

- LGD is an estimate of the economic loss rate if a default occurs during economic downturn conditions – LGD is determined based on industry data.

Wrong-way risk arises from positive expected correlation between EAD and PD to the same counterparty and the company seeks to avoid or appropriately mitigate this risk through collateral or other mitigants. Stress testing is utilised to identify any wrong-way risk in existing portfolios and risk mitigants and adjustments to capital may be employed to reflect any existing wrong-way risk.

The table below presents information on the components of the credit RWAs.

Credit RWAs	**31 December 2014 US$m**	**31 December 2013 US$m**
Derivatives	105,071	106,207
Commitments, guarantees and loans	2,413	1,473
Securities financing transactions	8,211	12,032
Equity investments	2,481	1,778
Other	9,170	5,998
Total Credit RWAs	**127,346**	**127,488**

STRATEGIC REPORT (continued)

7. Regulatory (continued)

Concentration risk

Under CRD IV, institutions are required to monitor and control their large exposures. The large exposure framework is designed to limit the risk of over-reliance on an individual counterparty or a group of connected counterparties. There is a general limit applied to all of the institution's exposures to a single counterparty or groups of connected counterparties, which is set at 25% of eligible capital. The framework includes reporting requirements, hard limits and additional concentration capital charges for trading book large exposures.

Market risk

Trading book positions are subject to market risk capital requirements which are based either on predetermined levels set by regulators or on internal models. The market risk regulatory capital rules require that a firm obtains the prior written approval of its regulators before using any internal model to calculate its risk-based capital requirement.

RWAs for market risk are computed using the following internal models: Value-at-Risk ('VaR'); Stressed VaR ('SVaR'); incremental risk; and comprehensive risk measure (for PRA purposes this is the All Price Risk Measure) the latter of which is subject to a floor. In addition, Standardised Rules, in accordance with CRD IV, are used to compute RWAs for market risk for certain securitised and non-securitised positions by applying risk-weighting factors predetermined by regulators to positions after applicable netting is performed. RWAs for market risk are the sum of each of these measures multiplied by 12.5. VaR is the potential loss in value of inventory positions, as well as certain other financial assets and financial liabilities, due to adverse market movements over a defined time horizon with a specified confidence level. For both risk management purposes and regulatory capital calculations the company uses a single VaR model which captures risks including those related to interest rates, equity prices, currency rates and commodity prices. However, VaR used for regulatory capital requirements ('regulatory VaR') differs from risk management VaR due to different time horizons and confidence levels (10-day and 99% for regulatory VaR vs. one-day and 95% for risk management VaR), as well as differences in the scope of positions on which VaR is calculated. SVaR is the potential loss in value of inventory positions during a period of significant market stress. Incremental risk is the potential loss in value of non-securitised inventory positions due to the default or credit migration of issuers of financial instruments over a one-year time horizon. All Price Risk is the potential loss in value, due to price risk and defaults, within the company's credit correlation positions.

The table below presents information on the components of the market RWAs.

Market RWAs	31 December 2014 US$m	31 December 2013 US$m
Model based capital requirement	15,236	15,112
Stressed VaR	13,625	12,125
Incremental risk	7,675	5,163
All Price Risk Measure	4,350	5,125
Standardised Rules	19,858	23,482
Securitisation	15,214	23,993
Total Market RWAs	**75,958**	**85,000**

Operational risk

GSI's capital requirements for operational risk are currently calculated under the Standardised Approach in accordance with PRA standards. The Standardised Approach requires companies to divide their activities into eight defined business lines or categories. Each business line is assigned a beta factor which is applied to the three-year average revenues of that business line (with certain prescribed exceptions, such as extraordinary income). Expenses are not included in the calculation. The sum of the individual business line requirements is multiplied by 12.5 to derive the operational RWAs.

STRATEGIC REPORT (continued)

7. Regulatory (continued)

Regulatory developments

The Basel Committee has recently issued several updates and consultative papers which propose further changes to capital regulations. In particular, it has finalised a revised standard approach for calculating RWAs for counterparty credit risk on derivatives exposures ("Standardised approach for measuring counterparty credit risk exposures," known as "SA-CCR"). In addition, it has published guidelines for measuring and controlling large exposures ("Supervisory framework for measuring and controlling large exposures"). The Basel Committee has also issued consultation papers on a "Fundamental review of the trading book," "Revisions to the securitisation framework", "Operational risk – Revisions to the simpler approaches," "Revisions to the standardised approach for credit risk" and "Capital floors: the design of a framework based on standardised approaches." The impact of all of these developments on the company (including RWAs and regulatory capital ratios) is subject to uncertainty until corresponding legislation is negotiated and implemented in the EU.

In December 2013, the final rules to implement the provisions of the Dodd-Frank Wall Street Reform and Consumer Protection Act ('Dodd-Frank Act') referred to as the "Volcker Rule" were adopted. GSI is subject to these provisions by virtue of being a subsidiary of GS Group.

The Volcker Rule prohibits "proprietary trading," but permits activities such as underwriting, market making and risk-mitigation hedging. GS Group is also required to calculate daily quantitative metrics on covered trading activities (as defined in the rule) and provide these metrics to regulators on a monthly basis. GS Group is required to be in compliance with the prohibition on proprietary trading and to develop an extensive compliance programme by July 2015. In December 2014, the Federal Reserve Board extended the compliance period through July 2016 for investments in, and relationships with, covered funds that were in place prior to 31 December 2013, and indicated that it intends to further extend the compliance period through July 2017. Based on current knowledge, the company, consistent with GS Group, does not expect the impact of the prohibition on proprietary trading to be material to its financial condition, results of operations or cash flows. However, the rule is highly complex and its eventual impact will not be fully known until market practices are further developed.

The Dodd-Frank Act and other reform initiatives proposed and announced by the U.S. federal bank regulatory agencies, the PRA and the FCA, the Basel Committee and other governmental entities and regulators (including the EU) are not in all cases consistent with one another, which adds further uncertainty to the future capital, leverage and liquidity requirements of GSI as a consolidating subsidiary of GS Group.

Regulatory leverage ratio

CRD IV introduced a new leverage ratio, which compares Tier 1 capital, as defined under CRD IV, to a measure of leverage exposure, defined as the sum of assets less Tier 1 capital deductions plus off-balance-sheet exposures (including a measure of derivatives exposures, securities financing transactions and commitments). The leverage ratio becomes effective for the company on 1 January 2018, although public disclosure requirements are effective for reporting periods from 1 January 2015.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties

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

Economic and market conditions

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

The company's financial performance is highly dependent on the environment in which its businesses operate. A favourable business environment is generally characterised by, among other factors, high global GDP growth, transparent, liquid and efficient capital markets, low inflation, high business and investor confidence, stable geopolitical conditions, regulatory certainty and strong business earnings. Unfavourable or uncertain economic and market conditions can be caused by: concerns about sovereign defaults; uncertainty in U.S. federal and EU fiscal or monetary policy; uncertainty about the timing and nature of regulatory reforms; declines in economic growth, business activity or investor or business confidence; limitations on the availability or increases in the cost of credit and capital; increases in inflation, interest rates, exchange rate volatility, default rates or the price of basic commodities; outbreaks of hostilities or other geopolitical instability; corporate, political or other scandals that reduce investor confidence in capital markets; extreme weather events or other natural disasters or pandemics; or a combination of these or other factors.

In 2008 and through early 2009, the financial services industry and the securities markets generally were materially and adversely affected by significant declines in the values of nearly all asset classes and by a serious lack of liquidity. Since 2011, concerns about European sovereign debt risk and its impact on the European banking system, and about changes in market conditions or actual changes in market conditions, have resulted, at times, in significant volatility while negatively impacting the levels of client activity.

General uncertainty about economic, political and market activities, and the timing and final implementation of regulatory reform, as well as weak consumer, investor and chief executive officer ('CEO') confidence resulting in large part from such uncertainty, continues to negatively impact client activity, which adversely affects many of the company's businesses. Periods of low volatility and periods of high volatility, combined with a lack of liquidity, have at times had an unfavourable impact on the company's market-making businesses.

The company's revenues and profitability and those of its competitors have been and will continue to be impacted by requirements relating to capital, leverage, minimum liquidity and long-term funding levels, requirements related to resolution and recovery planning, derivatives clearing and margin rules and levels of regulatory oversight, as well as limitations on whether and how certain business activities may be carried out by financial institutions. Although interest rates are at or near historically low levels, financial institution returns have also been negatively impacted by increased funding costs due in part to the withdrawal of perceived government support of such institutions in the event of future financial crises. In addition, liquidity in the financial markets may also be negatively impacted as market participants and market practices and structures adjust to new regulations.

In certain circumstances, market uncertainty or general declines in market or economic activity may affect client execution businesses by decreasing levels of overall activity or by decreasing volatility, but at other times market uncertainty and even declining economic activity may result in higher trading volumes or higher spreads or both.

Market uncertainty, volatility and adverse economic conditions, as well as declines in asset values, may cause clients to transfer their assets out of funds or other products or their brokerage accounts and result in reduced net revenues. To the extent that clients do not withdraw their funds, they may invest them in products that generate less fee income.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Regulation

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

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

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

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

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

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

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

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

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

Market volatility

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

The company's businesses have been and may be adversely affected by declining asset values. This is particularly true for those businesses in which the company has net long positions, receives fees based on the value of assets managed, or receives or posts collateral. Many of the company's businesses have net long positions in debt securities, loans, derivatives, mortgages, equities (including private equity and real estate) and most other asset classes. These include positions taken when the company acts as a principal to facilitate clients' activities, including exchange-based market-making activities, or commits large amounts of capital to maintain positions in interest rate and credit products, as well as through currencies, commodities and equities activities. Because substantially all of these investing and market-making positions are marked-to-market on a daily basis, declines in asset values directly and immediately impact earnings, unless exposures have been effectively hedged to such declines. In certain circumstances (particularly in the case of private equities or other securities that are not freely tradable or lack established and liquid trading markets), it may not be possible or economic to hedge such exposures and to the extent that this is done the hedge may be ineffective or may greatly reduce the company's ability to profit from increases in the values of the assets. Sudden declines and significant volatility in the prices of assets may substantially curtail or eliminate the trading markets for certain assets, which may make it very difficult to sell, hedge or value such assets. The inability to sell or effectively hedge assets reduces the ability to limit losses in such positions and the difficulty in valuing assets may negatively affect the company's and its affiliates' capital, liquidity or leverage ratios, increase its funding costs and generally require additional capital.

In the company's exchange-based market-making activities, the company is obligated by stock exchange rules to maintain an orderly market, including by purchasing securities in a declining market. In markets where asset values are declining and in volatile markets, this results in losses and an increased need for liquidity.

Asset-based management fees are received based on the value of clients' portfolios managed by the company and, in some cases, incentive fees are also received based on increases in the value of such investments. Declines in asset values reduce the value of clients' portfolios which in turn reduce the fees earned for managing such assets.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Collateral is posted to support obligations and received to support the obligations of clients and counterparties in connection with client execution businesses. When the value of the assets posted as collateral declines, the party posting the collateral may need to provide additional collateral or, if possible, reduce its trading position. A classic example of such a situation is a margin call in connection with a brokerage account. Therefore, declines in the value of asset classes used as collateral mean that either the cost of funding positions is increased or the size of positions is decreased. If the company is the party providing collateral, this can increase costs and reduce profitability and if the company is the party receiving collateral, this can also reduce profitability by reducing the level of business done with clients and counterparties. In addition, volatile or less liquid markets increase the difficulty of valuing assets which can lead to costly and time-consuming disputes over asset values and the level of required collateral, as well as increased credit risk to the recipient of the collateral due to delays in receiving adequate collateral.

Liquidity

Liquidity is essential to the company's businesses. The company's liquidity could be impaired by an inability to access secured and / or unsecured debt markets, an inability to access funds from Group Inc. or other affiliates, an inability to sell assets or redeem investments or unforeseen outflows of cash or collateral. Any of these circumstances may arise due to circumstances that the company may be unable to control, such as a general market disruption or an operational problem that affects third parties or the company or its affiliates or even by the perception amongst market participants that the company, or other market participants, are experiencing greater liquidity risk. Furthermore, the company's ability to sell assets may be impaired if other market participants are seeking to sell similar assets at the same time, as is likely to occur in a liquidity or other market crisis or in response to changes to rules or regulations. In addition, financial institutions with which the company interacts may exercise set-off rights or the right to require additional collateral, including in difficult market conditions, which could further impair the company's access to liquidity.

The company is an indirect, wholly-owned operating subsidiary of Group Inc. and depends on Group Inc. for capital and funding. Group Inc. is a holding company and, therefore, depends on dividends, distributions and other payments from its subsidiaries to provide capital and funding to its other subsidiaries. Many of Group Inc.'s subsidiaries, including Group Inc.'s broker-dealer and bank subsidiaries, are subject to laws that restrict dividend payments or authorise regulatory bodies to block or reduce the flow of funds from those subsidiaries to Group Inc. In addition, Group Inc.'s broker-dealer subsidiaries are subject to restrictions on their ability to lend or transact with affiliates and to minimum regulatory capital requirements, as well as restrictions on their ability to use funds deposited with them in brokerage or bank accounts to fund their businesses. Additional restrictions on related party transactions, increased capital and liquidity requirements, the Federal Reserve Board's source of strength policy and additional limitations on the use of funds on deposit in bank or brokerage accounts, as well as lower earnings, can reduce the amount of funds available to Group Inc. to provide capital or funding to GSI.

Regulatory changes relating to liquidity may also negatively impact the company's results of operations and competitive position. Recently, numerous regulations have been adopted or proposed, and additional regulations are under consideration, to introduce more stringent liquidity requirements for large financial institutions. These regulations and others being considered address, among other matters, liquidity stress testing, minimum liquidity requirements, wholesale funding, restrictions on short-term debt issued by top-tier holding companies and requirements for structured notes. These may overlap with, and be impacted by, other regulatory changes, including new guidance on the treatment of brokered deposits and the capital, leverage and resolution and recovery frameworks applicable to large financial institutions, as well as proposals relating to minimum long-term debt requirements and bail-in capacity. Given the overlap and complex interactions among these new and prospective regulations, they may have unintended cumulative effects, and their full impact will remain uncertain until implementation of post-financial crisis regulatory reform is complete.

The degree to which these and other changes resulting from the financial crisis will have a long-term impact on the profitability of financial institutions will depend on the final interpretation and implementation of new regulations, the manner in which markets, market participants and financial institutions adapt to the new landscape, and the prevailing economic and financial market conditions. However, there is a risk that such changes will, at least in the near-term, continue to negatively impact the absolute level of revenues, profitability and return on equity of the company and at other financial institutions.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

The credit ratings of GSI and those of Group Inc. are important to the company's liquidity. A reduction in GSI and / or Group Inc.'s credit rating could adversely affect the company's liquidity and competitive position, increase borrowing costs, limit access to the capital markets or funding from Group Inc. or trigger obligations under certain provisions in some trading and collateralised financing contracts. Under these provisions, counterparties could be permitted to terminate contracts with GSI or Group Inc. or require additional collateral. Termination of trading and collateralised financing contracts could cause losses and impair liquidity by requiring Group Inc. or GSI to find other sources of financing or to make significant cash payments or securities movements.

GSI's and Group Inc.'s cost of obtaining long-term unsecured funding is directly related to both the credit spreads of GSI and Group Inc. Increases in credit spreads can significantly increase the cost of this funding. Changes in credit spreads are continuous, market-driven, and subject at times to unpredictable and highly volatile movements. Credit spreads are also influenced by market perceptions of GSI and / or Group Inc. creditworthiness. In addition, credit spreads may be influenced by movements in the costs to purchasers of credit default swaps referenced to long-term debt. The market for credit default swaps, although very large, has proven to be extremely volatile and at times may lack a high degree of structure or transparency.

Resolution and recovery planning

The UK implemented BRRD on 1 January 2015, which provides resolution authorities with the ability to recapitalise a failing entity by writing down its unsecured debt or converting it into equity. Such 'bail-in' powers are intended to enable the recapitalisation of a failing institution by allocating losses to its shareholders and unsecured debt holders. Refer to *Item 7 (Regulatory – Resolution and recovery planning)* for more information on the BRRD.

The circumstances in which a resolution authority would exercise its powers to apply these resolution tools – in particular, the 'bail-in' power – are uncertain. If these powers were to be exercised (or if there was a suggestion that they could be exercised) in respect of GSI, such exercise would likely have a material adverse effect on the value of debt investments in GSI, including a potential loss of some or all of such investment. Furthermore, the suggestion that such powers were to be exercised could also have an adverse impact on the value of such investments.

Credit markets

Widening credit spreads for the company or Group Inc., as well as significant declines in the availability of credit, have in the past adversely affected the company's ability to borrow on a secured and unsecured basis and may do so in the future. GSI obtains the majority of its unsecured funding from Group Inc., which funds itself on an unsecured basis by issuing long-term debt, by accepting deposits at its bank subsidiaries, by issuing hybrid financial instruments, or by obtaining bank loans or lines of credit. The company seeks to finance many of its assets on a secured basis. Any disruptions in the credit markets may make it harder and more expensive to obtain funding for businesses. If the company's available funding is limited or the company is forced to fund operations at a higher cost, these conditions may require curtailment of business activities and increase the cost of funding, both of which could reduce profitability, particularly in businesses that involve investing and market making.

Clients engaging in mergers and acquisitions often rely on access to the secured and unsecured credit markets to finance their transactions. A lack of available credit or an increased cost of credit can adversely affect the size, volume and timing of clients' merger and acquisition transactions – particularly large transactions – and adversely affect the company's financial advisory and underwriting businesses.

In addition, significant unrealised gains or losses may be incurred due solely to changes in GS Group's credit spreads or those of third parties, as these changes may affect the fair value of derivative instruments and the debt securities held or issued, which may in turn adversely affect results of operations and capital ratios.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Concentration of risk

Concentration of risk increases the potential for significant losses in market-making, underwriting and investing activities. The number and size of such transactions may affect results of operations in a given period. Moreover, because of concentration of risk, the company may suffer losses even when economic and market conditions are generally favourable for competitors. Disruptions in the credit markets can make it difficult to hedge these credit exposures effectively or economically. Rules adopted under the Dodd-Frank Act require issuers of asset-backed securities and any person who organises and initiates an asset-backed securities transaction to retain economic exposure to the asset, which is likely to significantly increase the cost to the company of engaging in securitisation activities. An inability to reduce credit risk by selling, syndicating or securitising these positions, including during periods of market stress, could negatively affect results of operations due to a decrease in the fair value of the positions, including due to the insolvency or bankruptcy of the borrower, as well as the loss of revenues associated with selling such securities or loans.

In the ordinary course of business, the company may be subject to a concentration of credit risk to a particular counterparty, borrower, issuer, including sovereign issuers, or geographical area or group of related countries, such as the EU. A failure or downgrade of, or default by, such entity could negatively impact the company’s businesses, perhaps materially, and the systems by which the company set limits and monitors the level of its credit exposure to individual entities, industries and countries may not function as anticipated. While the company’s activities expose it to many different industries and counterparties, a high volume of transactions is routinely executed with counterparties engaged in financial services activities, including brokers and dealers, commercial banks, clearing houses and exchanges. This has resulted in significant credit concentration with respect to these counterparties.

Credit quality

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

The company is also subject to the risk that its rights against third parties may not be enforceable in all circumstances. In addition, deterioration in the credit quality of third parties whose securities or obligations are held by the company including a deterioration in the value of collateral posted by third parties to secure their obligations to the company under derivatives contracts and loan agreements, could result in losses and / or adversely affect the company’s ability to rehypothecate or otherwise use those securities or obligations for liquidity purposes. A significant downgrade in the credit ratings of the company’s counterparties could also have a negative impact on the company’s results. While, in many cases, the company is permitted to require additional collateral from counterparties that experience financial difficulty, disputes may arise as to the amount of collateral the company is entitled to receive and the value of pledged assets. The termination of contracts and the foreclosure on collateral may subject the company to claims for the improper exercise of its rights. Default rates, downgrades and disputes with counterparties as to the valuation of collateral increase significantly in times of market stress and illiquidity.

As part of its clearing and prime brokerage business, the company finances clients’ positions and it could be held responsible for the defaults or the misconduct of its clients. Although credit exposures to specific clients and counterparties and to specific industries, countries and regions that are believed to present credit concerns are regularly reviewed, default risk may arise from events or circumstances that are difficult to detect or foresee.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Derivative transactions

The company is party to a large number of derivative transactions. Many of these derivative instruments are individually negotiated and non-standardised, which can make exiting, transferring or settling positions difficult. Many derivatives require that the company delivers to the counterparty the underlying security, loan or other obligation in order to receive payment. In a number of cases, the company does not hold or may not be able to obtain the underlying security, loan or other obligation. This could cause the company to forfeit the payments due to it under these contracts or result in settlement delays with the attendant credit and operational risk as well as increased costs to the company. Derivative transactions may also involve the risk that documentation has not been properly executed, that executed agreements may not be enforceable against the counterparty, or that obligations under such agreements may not be able to be netted against other obligations with such counterparty. In addition, counterparties may claim that such transactions were not appropriate or authorised.

The new International Swap and Derivatives Association ('ISDA') Protocol that took effect in January 2015 imposes a stay on certain cross-default and early termination rights within standard ISDA derivatives contracts between adhering parties in the event that one of them is subject to resolution in its home jurisdiction, including a resolution under the orderly liquidation authority in the United States. As a signatory to the ISDA Protocol, the company may not be able to exercise remedies against counterparties and, as this new regime has not yet been tested, the company may suffer risks or losses that it would not have expected to suffer if it could immediately close out transactions upon a termination event. The ISDA Protocol contemplates adoption of implementing regulations by various U.S. and non-U.S. regulators, and the ISDA Protocol's impact will depend on, among other things, how it is implemented.

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

Regulations have been proposed or adopted in various jurisdictions that provide for significantly increased regulation of and restrictions on derivative markets and transactions, including the introduction of standardised execution and clearing, margining and reporting requirements for OTC derivatives. The EU has established a set of new regulatory requirements for EU derivatives activities under the European Market Infrastructure Regulation, including requirements relating to portfolio reconciliation and reporting, which have already taken effect, as well as requirements relating to clearing and margining for uncleared derivatives, which are currently expected to be finalised during 2015. In addition, under the Dodd-Frank Act, the CFTC has proposed or adopted rules relating to swaps, swap dealers and major swap participants, and the U.S. Securities and Exchange Commission ('SEC') has proposed or adopted rules relating to security-based swaps, security-based swap dealers and major security-based swap participants.

The full application of new derivatives rules across different national and regulatory jurisdictions has not yet been fully established. In July 2013, the CFTC finalised guidance and timing on the cross-border regulation of swaps and announced that it had reached an understanding with the European Commission regarding the cross-border regulation of derivatives and the common goals underlying their respective regulations. In June 2014, the SEC issued rules and guidance on cross-border security-based swap activities. However, specific determinations of the extent to which regulators in each of the relevant jurisdictions will defer to regulations in other jurisdictions have not yet been completed. The full impact of the various regulatory developments in this area will not be known with certainty until all the rules are finalised and implemented and market practices and structures develop under the final rules.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Operational infrastructure

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

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

Financial, accounting, data processing or other operating systems and facilities may fail to operate properly or become disabled as a result of events that are wholly or partially beyond the company's control, such as a spike in transaction volume, adversely affecting the ability to process these transactions or provide these services. The company must continuously update these systems to support its operations and growth and to respond to changes in regulations and markets, and invest heavily in systemic controls and training to ensure that such transactions do not violate applicable rules and regulations or, due to errors in processing such transactions, adversely affect markets, clients and counterparties or the company itself. Systems enhancements and updates, as well as the requisite training, entail significant costs and create risks associated with implementing new systems and integrating them with existing ones.

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

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

The company's operations rely on the secure processing, storage and transmission of confidential and other information in its computer systems and networks. There have been several recent highly publicised cases involving financial services and consumer-based companies reporting the unauthorised disclosure of client or customer information, as well as cyber attacks involving the dissemination, theft and destruction of corporate information or other assets, as a result of failure to follow procedures by employees or contractors or as a result of actions by third-parties, including actions by foreign governments.

The company is regularly the target of attempted cyber attacks, including denial-of-service attacks, and must continuously monitor and develop its systems to protect its technology infrastructure and data from misappropriation or corruption. In addition, due to the interconnectivity with third-party vendors, central agents, exchanges, clearing houses and other financial institutions, the company could be adversely impacted if any of them is subject to a successful cyber attack or other information security event. Although the company takes protective measures and endeavours to modify them as circumstances warrant, its computer systems, software and networks may be vulnerable to unauthorised access, misuse, computer viruses or other malicious code and other events that could have a security impact. If one or more of such events occur, this potentially could jeopardise the company or its clients' or counterparties' confidential and other information processed and stored in, and transmitted through, the company's computer systems and networks, or otherwise cause interruptions or malfunctions in the company's, its clients', its counterparties' or third parties' operations, which could impact their ability to transact with the company or otherwise result in significant losses or reputational damage.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

The increased use of mobile and cloud technologies can heighten these and other operational risks. The company expects to expend significant additional resources on an ongoing basis to modify protective measures and to investigate and remediate vulnerabilities or other exposures, and the company may be subject to litigation and financial losses that are either not insured against or not fully covered through any insurance it maintains.

The company routinely transmits and receives personal, confidential and proprietary information by email and other electronic means. The company has discussed and worked with clients, vendors, service providers, counterparties and other third parties to develop secure transmission capabilities and protect against cyber attacks, but does not have, and may be unable to put in place, secure capabilities with all of its clients, vendors, service providers, counterparties and other third parties and it may not be able to ensure that these third parties have appropriate controls in place to protect the confidentiality of the information. An interception, misuse or mishandling of personal, confidential or proprietary information being sent to or received from a client, vendor, service provider, counterparty or other third party could result in legal liability, regulatory action and reputational harm.

Notwithstanding the proliferation of technology and technology-based risk and control systems, the company's businesses ultimately rely on human beings as their greatest resource, and from time-to-time, they make mistakes that are not always caught immediately by technological processes or by other procedures which are intended to prevent and detect such errors. These can include calculation errors, mistakes in addressing emails, errors in software development or implementation, or simple errors in judgement. The company strives to eliminate such human errors through training, supervision, technology and by redundant processes and controls. Human errors, even if promptly discovered and remediated, can result in material losses and liabilities for the company.

Technology

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

Risk management

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

Market conditions in recent years have involved unprecedented dislocations and highlight the limitations inherent in using historical data to manage risk. The models that GS Group, including GSI use to assess and control risk exposures reflect assumptions about the degrees of correlation or lack thereof among prices of various asset classes or other market indicators. In times of market stress or other unforeseen circumstances, market movements have limited effectiveness of the company's hedging strategies and have caused significant losses, and they may do so in the future.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Prudent risk management, as well as regulatory restrictions, may cause the company to limit its exposure to counterparties, geographic areas or markets, which may limit its business opportunities and increase the cost of funding or hedging activities.

New business initiatives

The company faces enhanced risks as new business initiatives lead it to transact with a broader array of clients and counterparties and expose it to new asset classes and new markets. A number of the company's recent and planned business initiatives and expansions of existing businesses may bring it into contact, directly or indirectly, with individuals and entities that are not within the company's traditional client and counterparty base and expose it to new asset classes and new markets. For example, the company continues to transact business and invest in new regions, including a wide range of emerging and growth markets. Deteriorating market conditions may lead to an increase in opportunities to acquire distressed assets and the company may determine opportunistically to increase its exposure to these types of assets.

These activities expose the company to new and enhanced risks, including risks associated with dealing with governmental entities, reputational concerns arising from dealing with less sophisticated counterparties and investors, greater regulatory scrutiny of these activities, increased credit-related, market, sovereign and operational risks, risks arising from accidents or acts of terrorism, and reputational concerns with the manner in which these assets are being operated or held. For example, there has recently been significant conflict between Russia and Ukraine, and sanctions have been imposed by the U.S. and EU on certain individuals and companies in Russia.

In conducting GSI's businesses and maintaining and supporting its global operations, the company is subject to risks of possible nationalisation, expropriation, price controls, capital controls, exchange controls and other restrictive governmental actions, as well as the outbreak of hostilities or acts of terrorism. In many countries, the laws and regulations applicable to the securities and financial services industries and many of the transactions in which the company is involved are uncertain and evolving, and it may be difficult to determine the exact requirements of local laws in every market. Any determination by local regulators that the company has not acted in compliance with the application of local laws in a particular market or a failure to develop effective working relationships with local regulators could have a significant and negative effect not only on GSI's businesses in that market but also on its reputation generally. The company is also subject to the enhanced risk that transactions it structures might not be legally enforceable in all cases.

The company's businesses and operations are increasingly expanding into new regions throughout the world, including emerging and growth markets, and this trend is expected to continue. Various emerging and growth market countries have experienced severe economic and financial disruptions, including significant devaluations of their currencies, defaults or threatened defaults on sovereign debt, capital and currency exchange controls, and low or negative growth rates in their economies, as well as military activity, civil unrest or acts of terrorism. The possible effects of any of these conditions include an adverse impact on the company's businesses and increased volatility in financial markets generally.

While business and other practices throughout the world differ, the company is subject in its operations worldwide to rules and regulations relating to corrupt and illegal payments, hiring practices and money laundering, as well as laws relating to doing business with certain individuals, groups and countries, such as the U.S. Foreign Corrupt Practices Act, the USA PATRIOT Act and U.K. Bribery Act.

While the company has invested and continues to invest significant resources in training and in compliance monitoring, the geographical diversity of operations, employees, clients and customers, as well as the vendors and other third parties that the company deals with, greatly increases the risk that it may be found in violation of such rules or regulations and any such violation could subject it to significant penalties or adversely affect its reputation.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

In addition, there have been a number of highly publicised cases around the world, involving actual or alleged fraud or other misconduct by employees in the financial services industry in recent years, and the company runs the risk that employee misconduct could occur. This misconduct has included and may include in the future the theft of proprietary information, including proprietary software. It is not always possible to deter or prevent employee misconduct and the precautions taken to prevent and detect this activity have not been and may not be effective in all cases.

Conflicts of interest

The potential for conflicts of interest is increasing and a failure to appropriately identify and address conflicts of interest could adversely affect the company's businesses. Due to the broad scope of GS Group's businesses and client base, the company regularly addresses potential conflicts of interest, including situations where services to a particular client or GS Group's own interests conflict, or are perceived to conflict, with the interests of another client, as well as situations where one or more of its businesses have access to material non-public information that may not be shared with other businesses within GS Group and situations where it may be a creditor of an entity with which GS Group also has an advisory or other relationship.

Extensive procedures and controls are in place that are designed to identify and address conflicts of interest, including those designed to prevent the improper sharing of information among businesses. However, appropriately identifying and dealing with conflicts of interest is complex and difficult, and the company's reputation, which is one of its most important assets, could be damaged and the willingness of clients to enter into transactions with the company may be affected if it fails, or appears to fail, to identify, disclose and deal appropriately with conflicts of interest. In addition, potential or perceived conflicts could give rise to litigation or regulatory enforcement actions.

Competition

The financial services industry and all of the company's businesses are intensely competitive, and are expected to remain so. The company competes on the basis of a number of factors, including transaction execution, products and services, innovation, reputation, creditworthiness and price. Over time, there has been substantial consolidation and convergence among companies in the financial services industry. This trend accelerated over recent years as a result of numerous mergers and asset acquisitions among industry participants. This trend has also hastened the globalisation of the securities and other financial services markets. As a result, the company has had to commit capital to support its operations and to execute large transactions. To the extent the company expands into new business areas and new geographic regions, it will face competitors with more experience and more established relationships with clients, regulators and industry participants in the relevant market, which could adversely affect its ability to expand. Governments and regulators have recently adopted regulations, imposed taxes, adopted compensation restrictions or otherwise put forward various proposals that have or may impact the company's ability to conduct certain of its businesses in a cost-effective manner or at all in certain or all jurisdictions, including proposals relating to restrictions on the type of activities in which financial institutions are permitted to engage. These or other similar rules, many of which do not apply to all the company's competitors, could impact its ability to compete effectively.

Pricing and other competitive pressures in the company's businesses have continued to increase, particularly in situations where some competitors may seek to increase market share by reducing prices. For example, in connection with investment banking and other assignments, the company has experienced pressure to extend and price credit at levels that may not always fully compensate it for the risks taken.

STRATEGIC REPORT (continued)

8. Principal risks and uncertainties (continued)

Personnel

The company's businesses may be adversely affected if it is unable to hire and retain qualified employees. The company's performance is largely dependent on the talents and efforts of highly skilled individuals; therefore, the company's continued ability to compete effectively in businesses, to manage businesses effectively and to expand into new businesses and geographic areas depends on its ability to attract new talented and diverse employees and to retain and motivate existing employees. Factors that affect the company's ability to attract and retain such employees include compensation and benefits, and a reputation as a successful business with a culture of fairly hiring, training and promoting qualified employees.

Competition from within the financial services industry and from businesses outside the financial services industry for qualified employees has often been intense. This is particularly the case in emerging and growth markets, where the company is often competing for qualified employees with entities that have a significantly greater presence or more extensive experience in the region.

The company's compensation practices are subject to review by, and the standards of, the PRA and the FCA. As a large financial institution, the company is subject to limitations on compensation practices (which may or may not affect competitors) by the PRA and the FCA and other regulators worldwide. These limitations, including any imposed by or as a result of future legislation or regulation, may require the company to alter compensation practices in ways that could adversely affect its ability to attract and retain talented employees.

Legal liability

Substantial legal liability or significant regulatory action against the company could have material adverse financial effects or cause significant reputational harm, which in turn could seriously harm business prospects. The company faces significant legal risks in its businesses, and the volume of claims and amount of damages and penalties claimed in litigation and regulatory proceedings against financial institutions remain high. GSI is, from time to time, subject to a number of other investigations and reviews by, and in some cases has received requests for documents and information from, various governmental and regulatory bodies and self-regulatory organisations relating to various aspects of the company's businesses and operations. From experience, legal claims by customers and clients increase in a market downturn and employment-related claims increase following periods of staff reduction.

Additionally, governmental entities are plaintiffs in certain of the legal proceedings in which the company is involved, and it may face future actions or claims by the same or other governmental entities. Recently, significant settlements by several large financial institutions with governmental entities have been publicly announced. The trend of large settlements with governmental entities may adversely affect the outcomes for other financial institutions in similar actions, especially where governmental officials have announced that the large settlements will be used as the basis or a template for other settlements.

Unforeseen or catastrophic events

The company may incur losses as a result of unforeseen or catastrophic events, including the emergence of a pandemic, such as Ebola, or other widespread health emergency (or concerns over the possibility of such an emergency), terrorist attacks, extreme weather events or other natural disasters. The occurrence of unforeseen or catastrophic events, including the emergence of a pandemic, or other widespread health emergency (or concerns over the possibility of such an emergency), terrorist attacks, extreme terrestrial or solar weather events or other natural disasters, could create economic and financial disruptions, and could lead to operational difficulties (including travel limitations) that could impair the company's ability to manage its businesses.

STRATEGIC REPORT (continued)

9. Overview and structure of risk management

Overview

Effective risk management is of primary importance to the success of the company. GSI has comprehensive risk management processes through which the risks associated with the company's business are monitored, evaluated and managed. These risks include market, credit, liquidity, operational, legal, regulatory and reputational risk exposures. Together with the GSI board of directors, an extensive cross-divisional committee membership structure with representation from senior management of GSI is key to the risk management culture throughout the company.

GSI's risk management framework, consistent with GS Group, is built around three core components: governance; processes; and people.

Governance. The company's senior managers lead and participate in risk-oriented committees, as do the leaders of its independent control and support functions, including those in compliance, controllers, credit risk management, human capital management, legal, market risk management, operations, operational risk management, tax, technology and treasury.

The company maintains strong communication about risk and has a culture of collaboration in decision-making among the revenue-producing units, independent control and support functions, committees and senior management. While the company believes that the first line of defence in managing risk rests with the managers in the revenue-producing units, it dedicates extensive resources to independent control and support functions in order to ensure a strong oversight structure and an appropriate segregation of duties. The company regularly reinforces a strong culture of escalation and accountability across all divisions and functions.

Processes. The company maintains various processes and procedures that are critical components of its risk management. First and foremost is the daily discipline of marking substantially all of the company's inventory to current market levels. The company carries its inventory at fair value, with changes in valuation reflected immediately in its risk management systems and in net revenue. The company does so because it believes this discipline is one of the most effective tools for assessing and managing risk and that it provides transparent and realistic insight into its financial exposures.

People. Even the best technology serves only as a tool for helping to make informed decisions in real time about the risks the company is taking. Ultimately, effective risk management requires the company's people to interpret risk data on an ongoing and timely basis and adjust risk positions accordingly. In both the revenue-producing units and the independent control and support functions, the experience of GSI's professionals, and their understanding of the nuances and limitations of each risk measure, guide the company in assessing exposures and maintaining them within prudent levels.

The company reinforces a culture of effective risk management in training and development programmes as well as the way performance is evaluated, and people are recognised and rewarded. Training and development programmes, including certain sessions led by the most senior leaders of GS Group and GSI, are focused on the importance of risk management, client relationships and reputational excellence. As part of the annual performance review process, reputational excellence is assessed, including how an employee exercises good risk management and reputational judgement, and adheres to the code of conduct and compliance policies. Review and reward processes are designed to communicate and reinforce to the company's professionals the link between behaviour and how people are recognised, the need to focus on clients and reputation, and the need to always act in accordance with the highest standards of GS Group.

STRATEGIC REPORT (continued)

9. Overview and structure of risk management (continued)

Structure

Oversight of risk in GSI is ultimately the responsibility of the GSI board of directors, who oversee risk both directly and through various committees. A series of committees within GSI with specific risk management mandates covering important aspects of the company's businesses also have oversight or decision-making responsibilities. The key committees with oversight of GSI's activities are described below.

European Management Committee ('EMC'). The EMC oversees all of GSI's activities in the region. Its membership includes the executive directors of GSI and senior managers from the revenue-producing divisions and control and support functions. The EMC reports to the GSI board of directors.

EMEA Audit, Business Standards & Compliance Committee ('EABSCC'). The EABSCC assists the directors and senior management of the company in the oversight of business standards, compliance, operational and reputational risks and in the review of processes for ensuring the suitability and effectiveness of the systems and controls of the company in the region. Its membership includes senior managers from the revenue-producing divisions and independent control and support functions. The EABSCC also has responsibility for overseeing the external audit arrangements and review of internal audit activities. The EABSCC reports to the EMC and to the GSI board of directors.

GSI Risk Committee. The GSI Risk Committee is responsible for the on-going monitoring and control of all financial risks associated with GSI's activities. This includes reviewing key financial and risk metrics, including but not limited to profit and loss, capital (including ICAAP), funding, liquidity, credit risk, market risk, operational risk, price verification and stress tests. The GSI Risk Committee approves VaR, credit, liquidity and regulatory capital limits. The GSI Risk Committee reports to the GSI board of directors.

GS Group risk governance

The comprehensive global risk governance framework in place at the GS Group level forms an integral part of the risk management process at GSI. GS Group has established a series of committees with specific risk management mandates. Committees with oversight of matters relevant to GSI include representation from GSI's senior management. The primary GS Group risk and oversight committees are described below.

Management Committee. The Management Committee oversees the global activities of GS Group, including the group's independent control and support functions. The committee is comprised of the most senior leaders of GS Group, and is chaired by the group's CEO. The co-CEOs of GSI are both members of the committee.

Firmwide Client and Business Standards Committee. The Firmwide Client and Business Standards Committee assesses and makes determinations regarding business standards and practices, reputational risk management, client relationships and client service, is chaired by the group's president and chief operating officer, and reports to the Management Committee. The membership includes representation from senior management in GSI's revenue-producing divisions and control and support functions.

Firmwide Risk Committee. The Firmwide Risk Committee is globally responsible for the ongoing monitoring and management of the group's financial risks. The Firmwide Risk Committee approves firmwide, product, divisional and business-level limits for both market and credit risks. The membership includes representation from senior management in GSI's revenue-producing divisions and control and support functions.

STRATEGIC REPORT (continued)

10. Liquidity risk management

Overview (audited)

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

Liquidity risk management principles (audited)

GSI manages liquidity risk according to the following principles:

- Liquidity – maintain substantial liquidity (GCLA, previously GCE) to meet a broad range of potential cash outflows and collateral needs in a stressed environment;

- Asset-liability management – assess anticipated holding periods for the company's assets and their expected liquidity in a stressed environment, manage maturities and diversity of funding across markets, products and counterparties, and seek to maintain liabilities of appropriate tenor relative to the asset base; and

- Contingency funding plan ('CFP') – GSI maintains a CFP, which is an addendum to the GS Group CFP. The contingency funding plan provides a framework for analysing and responding to a liquidity crisis situation or periods of market stress. This framework sets forth the plan of action to fund normal business activity in emergency and stress situations. These principles are set out in more detail below.

Liquidity

The company's most important liquidity policy is to pre-fund its estimated potential cash and collateral needs during a liquidity crisis and hold this liquidity in the form of unencumbered, highly liquid securities and cash. The company believes that the securities held in its GCLA would be readily convertible to cash in a matter of days, through liquidation, by entering into repurchase agreements or from maturities of securities purchased under agreements to resell ('resale agreements'), and that this cash would allow it to meet immediate obligations without needing to sell other assets or depend on additional funding from credit-sensitive markets.

As at 31 December 2014, the fair value of the securities and certain overnight cash deposits included in GSI's GCLA totalled US$54.2 billion (2013: US$45.8 billion). During the year the company, consistent with GS Group, introduced an enhanced Intraday Liquidity Model and as a result the company increased the amount of GCLA held.

The table below presents the average daily fair value of GSI's GCLA by asset class.

	Average daily fair value of GCLA	
	Year Ended 31 December 2014	**Year Ended 31 December 2013**
	US$m	**US$m**
Overnight cash deposits	906	1,778
U.S. government obligations	15,322	9,632
French government obligations	9,073	10,864
United Kingdom government obligations	15,614	9,482
German government obligations	6,896	9,217
Japanese government obligations	2,086	41
Total	**49,897**	**41,014**

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

The company strictly limits excess GCLA to the following narrowly defined list of securities and cash because they are highly liquid, even in a difficult funding environment. The following securities and cash balances are eligible for inclusion in the GCLA: (i) unencumbered U.S. government obligations; (ii) unencumbered German, French, Japanese and United Kingdom government obligations; and (iii) certain overnight cash deposits in U.S. dollars and other highly liquid currencies. The company does not include other potential sources of liquidity, such as less liquid unencumbered securities or committed credit facilities, in the GCLA.

GSI's GCLA reflects the following principles:

- The first days or weeks of a liquidity crisis are the most critical to a company's survival;

- Focus must be maintained on all potential cash and collateral outflows, not just disruptions to financing flows. The company's businesses are diverse, and its liquidity needs are determined by many factors, including market movements, collateral requirements and client commitments, all of which can change dramatically in a difficult funding environment;

- During a liquidity crisis, credit-sensitive funding, including unsecured debt and some types of secured financing agreements, may be unavailable, and the terms (e.g. interest rates, collateral provisions and tenor) or availability of other types of secured financing may change; and

- As a result of the company's policy to pre-fund liquidity that it estimates may be needed in a crisis, GSI holds more unencumbered securities and has larger debt balances than it would otherwise require. GSI believes that its liquidity is stronger with greater balances of highly liquid unencumbered securities, even though it increases total assets and funding costs.

The company believes that GCLA provides a resilient source of funds that would be available in advance of potential cash and collateral outflows and gives significant flexibility in managing through a difficult funding environment.

In order to determine the appropriate size of the company's GCLA, an internal liquidity model is used, referred to as the Modelled Liquidity Outflow ('MLO'), which captures and quantifies the company's liquidity risks. Other factors are considered including, but not limited to, an assessment of potential intraday liquidity needs through an additional internal liquidity model, referred to as the Intraday Liquidity Model ('ILM'), and a qualitative assessment of the condition of the financial markets and of the company.

The company's GCLA is distributed across issuers and clearing agents to provide sufficient operating liquidity to ensure timely settlement in all major markets, even in a difficult funding environment.

The company maintains GCLA to enable it to meet current and potential liquidity requirements. The minimum GCLA required, as calculated by the MLO and the ILM, is held by the company directly and is intended for use only by GSI to meet its liquidity requirements, and is assumed not to be available to Group Inc. In addition to GCLA held in GSI, GS Group holds a portion of global GCLA directly at Group Inc., which in some circumstances may be additionally provided to GSI or other major subsidiaries.

In addition to GCLA, the company has a significant amount of other unencumbered cash and financial instruments owned, at fair value, including other government obligations, high-grade money market securities, corporate obligations, marginable equities, loans and cash deposits not included in the GCLA. The fair value of these assets averaged US$30.5 billion for 2014 and US$29.6 billion for 2013. GSI does not consider these assets liquid enough to be eligible for inclusion in its GCLA.

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

Modelled Liquidity Outflow. The MLO is based on a scenario that includes both a market-wide stress and a GS Group-specific stress, characterised by the following qualitative elements:

- Severely challenged market environments, including low consumer and corporate confidence, financial and political instability, adverse changes in market values, including potential declines in equity markets and widening of credit spreads; and

- An idiosyncratic crisis potentially triggered by material losses, reputational damage, litigation, executive departure, and / or a ratings downgrade.

The following are the critical modelling parameters of the MLO:

- Liquidity needs over a 30-day scenario;

- A two-notch downgrade of the long-term senior unsecured credit ratings of Group Inc. and its rated subsidiaries, including GSI;

- A combination of contractual outflows, such as upcoming maturities of unsecured debt, and contingent outflows (e.g. actions though not contractually required, may be deemed necessary in a crisis). GSI assumes most contingent outflows will occur within the initial days and weeks of a crisis;

- No issuance of equity or unsecured debt; and

- No asset liquidation, other than the GCLA.

The MLO is calculated and reported to senior management on a daily basis. The company regularly refines the model to reflect changes in market or economic conditions and the company's business mix.

The potential contractual and contingent cash and collateral outflows covered in the MLO include the following items.

External unsecured funding

- Contractual: All upcoming maturities of unsecured long-term debt and other unsecured funding products. GSI assumes that it will be unable to issue new unsecured debt or rollover any maturing debt.

- Contingent: Repurchases of outstanding long-term debt and hybrid financial instruments in the ordinary course of business as a market maker.

Secured funding

- Contractual: A portion of upcoming contractual maturities of secured funding due to either the inability to refinance or the ability to refinance only at wider haircuts (i.e. on terms which require the company to post additional collateral). Assumptions reflect, among other factors, the quality of the underlying collateral, counterparty roll probabilities (the company's assessment of the counterparty's likelihood of continuing to provide funding on a secured basis at the maturity of the trade) and counterparty concentration.

- Contingent: Adverse changes in value of financial assets pledged as collateral for financing transactions, which would necessitate additional collateral postings under those transactions.

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

OTC derivatives

- Contingent: Collateral postings to counterparties due to adverse changes in the value of the company's OTC derivatives, excluding those that are cleared and settled through central counterparties ('OTC-cleared').

- Contingent: Other outflows of cash or collateral related to OTC derivatives, excluding OTC-cleared, including the impact of trade terminations, collateral substitutions, collateral disputes, loss of rehypothecation rights, collateral calls or termination payments required by a two-notch downgrade in Group Inc. and GSI's credit ratings, and collateral that has not been called by counterparties, but is available to them.

Exchange-traded and OTC-cleared derivatives

- Contingent: Variation margin postings required due to adverse changes in the value of outstanding exchange-traded and OTC-cleared derivatives.

- Contingent: An increase in initial margin and guarantee fund requirements by derivative clearing houses.

Customer cash and securities

- Contingent: Liquidity outflows associated with the company's prime brokerage business, including withdrawals of customer credit balances, and a reduction in customer short positions, which may serve as a funding source for long positions.

Firm securities

- Contingent: Liquidity outflows associated with a reduction or composition change in firm short positions, which may serve as a funding source for long positions.

Other

- Other upcoming large cash outflows, such as tax payments.

Intraday Liquidity Model. The company's ILM measures the company's intraday liquidity needs using a scenario analysis characterised by the same qualitative elements as the MLO. The model assesses the risk of increased intraday liquidity requirements during a scenario where access to sources of intraday liquidity may become constrained.

The following are key modelling elements of the ILM:

- Liquidity needs over a one-day settlement period;

- Delays in receipt of counterparty cash payments;

- A reduction in the availability of intraday credit lines at the company's third-party clearing agents; and

- Higher settlement volumes due to an increase in activity.

The company's model is regularly refined to reflect changes in market conditions, business mix and operational processes.

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

Asset-liability management

The company's liquidity risk management policies are designed to ensure it has a sufficient amount of financing, even when funding markets experience persistent stress. GSI seeks to maintain a long-dated and diversified external funding profile, taking into consideration the characteristics and liquidity profile of its assets. In addition, the company sources unsecured funding from GS Group and other affiliates. Refer to *Item 6 (Balance sheet and funding sources – Funding sources)* for additional details.

GSI's approach to asset-liability management includes:

- Conservatively managing the overall characteristics of its funding book, with a focus on maintaining long-term, diversified sources of funding in excess of current requirements – refer to *Item 6 (Balance sheet and funding sources – Funding sources)* for additional details;

- Actively managing and monitoring its asset base, with particular focus on the liquidity, holding period and its ability to fund assets on a secured basis – this enables the company to determine the most appropriate funding products and tenors – refer to *Item 6 (Balance sheet and funding sources – Balance sheet management)* for more detail on the balance sheet management process and *Item 6 (Balance sheet and funding sources – Funding sources – Secured funding)* for more detail on asset classes that may be harder to fund on a secured basis; and

- Raising secured and unsecured financing that has a long tenor relative to the liquidity profile of its assets – this reduces the risk that liabilities will come due in advance of the company's ability to generate liquidity from the sale of assets – because GSI maintains a highly liquid balance sheet, the holding period of certain assets may be materially shorter than their contractual maturity dates.

The goal is to ensure the company maintains sufficient liquidity to fund its assets and meet its contractual and contingent obligations in normal times as well as during periods of market stress. Through the dynamic balance sheet management process (refer to *Item 6 (Balance sheet and funding sources – Balance sheet management)*), actual and projected asset balances are used to determine secured and unsecured funding requirements. In a liquidity crisis, the company would first use its GCLA in order to avoid reliance on asset sales (other than its GCLA). However, the company recognises that orderly asset sales may be prudent or necessary in a severe or persistent liquidity crisis.

Contingency funding plan

The GS Group contingency funding plan ('CFP') sets out the plan of action the company would use to fund business activity in crisis situations and periods of market stress. The CFP is prepared on a GS Group basis, and has a GSI-specific addendum. The CFP outlines a list of potential risk factors, key reports and metrics that are reviewed on an ongoing basis to assist in assessing the severity of, and managing through, a liquidity crisis and / or market dislocation. The CFP also describes the company's potential responses if assessments indicate that the company has entered a liquidity crisis, which includes pre-funding for what the company estimates will be its potential cash and collateral needs as well as utilising secondary sources of liquidity. Mitigants and action items to address specific risks which may arise are also described and assigned to individuals responsible for execution.

The CFP identifies key groups of individuals to foster effective coordination, control and distribution of information, all of which are critical in the management of a crisis or period of market stress. The CFP also details the responsibilities of these groups and individuals, which include making and disseminating key decisions, coordinating all contingency activities throughout the duration of the crisis or period of market stress, implementing liquidity maintenance activities and managing internal and external communication.

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

Liquidity regulatory framework

The Basel Committee's international framework for liquidity risk measurement, standards and monitoring calls for imposition of a liquidity coverage ratio ('LCR'), designed to ensure that banks and bank holding companies maintain an adequate level of unencumbered high-quality liquid assets based on expected cash outflows under an acute liquidity stress scenario, and a net stable funding ratio ('NSFR'), designed to promote more medium- and long-term funding of the assets and off-balance-sheet activities of these entities over a one-year time horizon. In 2014, the Basel Committee issued the final rules on the calculation of the NSFR which requires banks and bank holding companies to maintain a stable funding profile in relation to the composition of their assets and off-balance-sheet activities. The LCR will be effective in the EU on 1 October 2015, with a phase-in period whereby firms would have a 60% minimum in 2015 which would be raised each year until 2018. The NSFR will be effective on 1 January 2018.

The implementation of these standards could impact the company's liquidity and funding requirements and practices.

Credit ratings

The table below presents the unsecured credit ratings and outlook of GSI and Group Inc. as at 31 December 2014. During the fourth quarter of 2014, Standard & Poor's Rating Services raised its outlook of the company from negative to stable as a result of its review of the company's operating trends in the current regulatory environment.

	Standard & Poor's Rating Services	Moody's Investors Service	Fitch Ratings, Inc.
GSI			
Short-term debt	A-1	P-1	F1
Long-term debt	A	A2	A
Ratings outlook	Stable	Stable[1]	Stable
Group Inc.			
Short-term debt	A-2	P-2	F1
Long-term debt	A-	Baa1	A
Subordinated debt	BBB+	Baa2	A-
Trust preferred	BB	Baa3	BBB-
Preferred stock	BB	Ba2	BB+
Ratings outlook	Negative	Stable[1]	Stable

1. On 17 March 2015, Moody's Investors Service placed the long-term debt ratings of GSI and Group Inc. under review for upgrade and the non-cumulative preferred stock rating of Group Inc. under review for upgrade following the publication of its new bank rating methodology.

STRATEGIC REPORT (continued)

10. Liquidity risk management (continued)

GSI relies on the debt capital markets to fund a portion of its day-to-day operations and the cost and availability of debt financing is influenced by its credit rating and that of Group Inc. Credit ratings are also important when GSI is competing in certain markets, such as OTC derivatives, and when GSI seeks to engage in longer-term transactions.

The company believes credit ratings are primarily based on the credit rating agencies' assessment of:

- The company's liquidity, market, credit and operational risk management practices;
- The level and variability of the company's earnings;
- The company's capital base;
- The GS Group franchise, reputation and management;
- The company's corporate governance;
- The external operating environment, including, in some cases, the assumed level of government support or other systematic support; and
- The importance of GSI to the GS Group.

Certain of the company's derivatives have been transacted under bilateral agreements with counterparties who may require GSI to post collateral or terminate the transactions based on changes in the credit ratings of either GSI and / or Group Inc. The company assesses the impact of these bilateral agreements by determining the collateral or termination payments that would occur assuming a downgrade by all rating agencies of both Group Inc. and GSI simultaneously and of each entity individually. A downgrade by any one rating agency, depending on the agency's relative ratings of Group Inc. and GSI at the time of the downgrade, may have an impact which is comparable to the impact of a downgrade by all rating agencies.

The company allocates a portion of its GCLA to ensure that it would be able to make the additional collateral or termination payments that may be required in the event of a two-notch reduction in Group Inc. and / or GSI's long-term credit ratings, as well as collateral that has not been called by counterparties, but is available to them. The table below presents the additional collateral or termination payments related to the company's net derivative liabilities under bilateral agreements that could have been called at the reporting date by counterparties in the event of a one-notch and two-notch downgrade in Group Inc. and / or GSI's credit ratings.

	31 December 2014 US$m	31 December 2013 US$m
Additional collateral or termination payments for a one-notch downgrade	294	362
Additional collateral or termination payments for a two-notch downgrade	1,295	1,545

<u>Maturity of financial liabilities</u>

Refer to *note 29e to the financial statements* for a maturity analysis of the company's financial liabilities.

STRATEGIC REPORT (continued)

11. Market risk management

Overview (audited)

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

- Interest rate risk: results from exposures to changes in the level, slope and curvature of yield curves, the volatilities of interest rates, mortgage prepayment speeds and credit spreads;
- Equity price risk: results from exposures to changes in prices and volatilities of individual equities, baskets of equities and equity indices;
- Currency rate risk: results from exposures to changes in spot prices, forward prices and volatilities of currency rates; and
- Commodity price risk: results from exposures to changes in spot prices, forward prices and volatilities of commodities, such as crude oil and metals.

Market risk management process (audited)

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

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

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

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

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

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

STRATEGIC REPORT (continued)

11. Market risk management (continued)

Risk measures

Market Risk Management produces risk measures and monitors them against market risk limits set by the GSI Risk Committee. These measures reflect an extensive range of scenarios and the results are aggregated by business at the company level.

A variety of risk measures are used to estimate the size of potential losses for both moderate and more extreme market moves over both short-term and long-term time horizons. Primary risk measures are VaR, used for shorter-term periods, and stress tests. The GSI risk report details key risks, drivers and changes for each business, and is distributed daily to senior management of both the revenue-producing units and independent control and support functions.

Value-at-Risk

VaR is the potential loss in value of financial instruments due to adverse market movements over a defined time horizon with a specified confidence level. A one-day time horizon with a 95% confidence level is typically employed. The VaR model is a single model that captures risks including interest rates, equity prices, currency rates and commodity prices. As such, VaR facilitates comparison across portfolios of different risk characteristics. VaR also captures the diversification of aggregated risk across GSI.

There are inherent limitations to VaR and therefore a variety of risk measures are used in the market risk management process. Inherent limitations to VaR include:

- VaR does not estimate potential losses over longer time horizons where moves may be extreme;
- VaR does not take account of the relative liquidity of different risk positions; and
- Previous moves in market risk factors may not produce accurate predictions of all future market moves.

When calculating VaR, historical simulations with full valuation of approximately 70,000 market factors are used. VaR is calculated at a position level based on simultaneously shocking the relevant market risk factors for that position. A sample from five years of historical data is taken to generate the scenarios for the VaR calculation. The historical data is weighted so that the relative importance of the data reduces over time. This gives greater importance to more recent observations and reflects current asset volatilities, which improves the accuracy of estimates of potential loss. As a result, even if positions included in VaR were unchanged, VaR would increase with increasing market volatility and vice versa.

Given its reliance on historical data, VaR is most effective in estimating risk exposures in markets in which there are no sudden fundamental changes or shifts in market conditions.

The VaR measure does not include:

- Positions that are best measured and monitored using sensitivity measures; and
- The impact of changes in counterparty and GS Group’s credit spreads on derivatives, as well as changes in its credit spreads on unsecured borrowings, which are designated at fair value through profit or loss.

STRATEGIC REPORT (continued)

11. Market risk management (continued)

Stress testing

Stress testing is a method of determining the effect on GS Group of various hypothetical stress scenarios. GS Group uses stress testing to examine risks of specific portfolios as well as the potential impact of significant risk exposures across GS Group, and the impact specifically on GSI. It uses a variety of stress testing techniques to calculate the potential loss from a wide range of market moves on GSI's portfolios, including sensitivity analysis, scenario analysis and GSI stress tests. The results of the various stress tests are analysed together for risk management purposes.

Sensitivity analysis is used to quantify the impact of a market move in a single risk factor across all positions (e.g. equity prices or credit spreads) using a variety of defined market shocks, ranging from those that could be expected over a one-day time horizon up to those that could take many months to occur. Sensitivity analysis is also used to quantify the impact of the default of a single corporate entity, which captures the risk of large or concentrated exposures.

Scenario analysis is used to quantify the impact of a specified event, including how the event impacts multiple risk factors simultaneously. For example, for sovereign stress testing GSI calculates potential direct exposure associated with its sovereign inventory as well as the corresponding debt, equity and currency exposures associated with its non-sovereign inventory that may be impacted by the sovereign distress. When conducting scenario analysis, GS Group typically considers a number of possible outcomes for each scenario, ranging from moderate to severely adverse market impacts. In addition, these stress tests are constructed using both historical events and forward-looking hypothetical scenarios.

Stress testing combines market, credit, operational and liquidity risks into a single combined scenario and reviews the potential impact across GS Group and on GSI. Stress tests are primarily used to assess capital adequacy as part of the capital planning and stress testing process; however, it is also ensured that stress testing is integrated into the risk governance framework. This includes selecting appropriate scenarios to use for the capital planning and stress testing process.

Unlike VaR measures, which have an implied probability because they are calculated at a specified confidence level, there is generally no implied probability that GS Group's stress test scenarios will occur. Instead, stress tests are used to model both moderate and more extreme moves in underlying market factors. When estimating potential loss, it is generally assumed that positions cannot be reduced or hedged (although experience demonstrates that it is generally possible to do so).

Stress test scenarios are conducted on a regular basis as part of the routine risk management process and on an *ad hoc* basis in response to market events or concerns. Stress testing is an important part of the risk management process because it allows the company to quantify its exposure to tail risks, highlight potential loss concentrations, undertake risk / reward analysis and assess and mitigate its risk positions.

Limits

Risk limits are used at various levels in GS Group (including entity, product and business) to govern risk appetite by controlling the size of its exposures to market risk. Limits for GSI are set based on VaR and on a range of stress tests relevant to the company's exposures. Limits are reviewed frequently and amended on a permanent or temporary basis to reflect changing market conditions, business conditions or tolerance for risk.

The GSI Risk Committee sets market risk limits at an overall, product and business level. The purpose of the limits is to assist senior management in controlling the overall risk profile. Business level limits are designed to set the desired maximum amount of exposure that may be managed by any particular business on a day-to-day basis without additional levels of senior management approval, effectively leaving day-to-day trading decisions to individual desk managers and traders. Accordingly, business level limits are a management tool designed to ensure appropriate escalation rather than to establish maximum risk tolerance. Business level limits also distribute risk among various businesses in a manner that is consistent with their level of activity and client demand, taking into account the relative performance of each area.

STRATEGIC REPORT (continued)

11. Market risk management (continued)

Market risk limits are monitored daily by Market Risk Management, which is responsible for identifying and escalating, on a timely basis, instances where limits have been exceeded. The limits that are set by the GSI Risk Committee are subject to the same scrutiny and limit escalation policy as the GS Group limits.

When a risk limit has been exceeded (e.g. due to changes in market conditions, such as increased volatilities or changes in correlations) it is reported to the GSI Risk Committee and a discussion takes place with the relevant desk managers, after which either the risk position is reduced or the risk limit is temporarily or permanently increased.

Model review and validation

The VaR and stress testing models are subject to review and validation by GS Group's independent model validation group. This review includes:

- A critical evaluation of the model, its theoretical soundness and adequacy for intended use;
- Verification of the testing strategy utilised by the model developers to ensure that the model functions as intended; and
- Verification of the suitability of the calculation techniques incorporated in the model.

The VaR and stress testing models are regularly reviewed and enhanced in order to incorporate changes in the composition of positions included in market risk measures, as well as variations in market conditions. Prior to implementing significant changes to VaR assumptions and / or models, model validation and test runs are performed. Significant changes to the VaR and stress testing models are reviewed with GS Group's chief risk officer and chief financial officer, as well as approved by GS Group's Firmwide Risk Committee and, where appropriate, the GSI Risk Committee.

The VaR model is applied consistently across GS Group, including GSI, and the accuracy of the VaR model is evaluated through daily backtesting (i.e. by comparing daily trading net revenues to the VaR measure calculated as of the prior business day) at the GS Group and GSI level and for each of GS Group's businesses.

Systems

GS Group has made a significant investment in technology to monitor market risk including:

- An independent calculation of VaR and stress measures;
- Risk measures calculated at individual position levels;
- Attribution of risk measures to individual risk factors of each position;
- The ability to report many different views of the risk measures (e.g. by desk, business, product type or legal entity); and
- The ability to produce *ad hoc* analyses in a timely manner.

STRATEGIC REPORT (continued)

11. Market risk management (continued)

Metrics (audited)

The tables below present, by risk category, average daily VaR and year-end VaR, as well as the high and low VaR for the year. Diversification effect in the tables below represents the difference between total VaR and the sum of the VaRs for the four risk categories. This effect arises because the four market risk categories are not perfectly correlated.

	Average daily VaR	
	Year Ended 31 December 2014	**Year Ended 31 December 2013**
	US$m	**US$m**
Risk categories:		
Interest rates	19	26
Equity prices	18	17
Currency rates	5	5
Commodity prices	-	-
Diversification effect	(12)	(12)
Total	**30**	**36**

The company's average daily VaR decreased to US$30 million in 2014 from US$36 million in 2013, primarily reflecting a decrease in the interest rates category due to decreased exposures and lower levels of volatility.

Year-end VaR and high and low VaR

			High	**Low**
	31 December 2014	**31 December 2013**	**Year Ended 31 December 2014**	**Year Ended 31 December 2014**
	US$m	**US$m**	**US$m**	**US$m**
Risk categories:				
Interest rates	27	29	28	14
Equity prices	11	20	36	11
Currency rates	4	7	10	3
Commodity prices	1	-	2	-
Diversification effect	(15)	(18)		
Total	**28**	**38**	**46**	**21**

The company's daily VaR decreased to US$28 million as at 31 December 2014 from US$38 million as at 31 December 2013, primarily reflecting a decrease in the equity prices category principally due to decreased exposures.

During 2014 and 2013, the company's VaR risk limit was not exceeded, raised or reduced.

STRATEGIC REPORT (continued)

11. Market risk management (continued)

Sensitivity measures (audited)

Certain portfolios and individual positions are not included in VaR because VaR is not the most appropriate risk measure for these positions. The market risk of these positions is determined by estimating the potential reduction in net revenue of a 10% decline in the underlying asset value.

10% sensitivity measures

	31 December 2014 US$m	31 December 2013 US$m
Asset categories:		
Equity	16.0	26.9
Debt	0.3	0.5
Total	**16.3**	**27.4**

The company's 10% sensitivity measures decreased to US$16.3 million as at 31 December 2014 from US$27.4 million as at 31 December 2013, primarily reflecting a decrease in the equity asset category due to a reduction in private equity positions.

12. Credit risk management

Overview (audited)

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

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

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

STRATEGIC REPORT (continued)

12. Credit risk management (continued)

Credit risk management process (audited)

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

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

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

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

Risk measures and limits

Credit risk is measured based on the potential loss in an event of non-payment by a counterparty. For derivatives and securities financing transactions, the primary measure is potential exposure, which is the estimate of the future exposure that could arise over the life of a transaction based on market movements within a specified confidence level. Potential exposure takes into account netting and collateral arrangements. Credit risk is also monitored in terms of current exposure, which is the amount presently owed to the company after taking into account applicable netting and collateral.

Credit limits are used at various levels (counterparty, economic group, industry, country) to control the size of the company's credit exposures. Limits for counterparties and economic groups are reviewed regularly and revised to reflect changing risk appetites for a given counterparty or group of counterparties. Limits for industries and countries are based on the company's risk tolerance and are designed to allow for regular monitoring, review, escalation and management of credit risk concentrations.

STRATEGIC REPORT (continued)

12. Credit risk management (continued)

Stress tests / scenario analysis

Regular stress tests are used to calculate the credit exposures, including potential concentrations that would result from applying shocks to counterparty credit ratings or credit risk factors (e.g. currency rates, interest rates, equity prices). These shocks include a wide range of moderate and more extreme market movements. Some of the stress tests include shocks to multiple risk factors, consistent with the occurrence of a severe market or economic event. In the case of sovereign default, Credit Risk Management estimates the direct impact of the default on the company's credit exposures, changes to the company's risk exposures arising from potential market moves in response to the default, and the impact of credit market deterioration on corporate borrowers and counterparties that may result from the sovereign default. Unlike potential exposure, which is calculated within a specified confidence level, with a stress test there is generally no assumed probability of these events occurring.

Stress tests are run on a regular basis as part of the company's routine risk management processes and the company conducts tailored stress tests on an *ad hoc* basis in response to market developments. Stress tests are regularly conducted jointly with the company's market and liquidity risk functions.

Risk mitigants

To reduce the credit exposures on derivatives and securities financing transactions, the company may enter into netting agreements with counterparties that permit it to offset receivables and payables with such counterparties. The company may also reduce credit risk with counterparties by entering into agreements that enable it to obtain collateral from them on an upfront or contingent basis and / or terminate transactions if the counterparty's credit rating falls below a specified level. The company monitors the fair value of the collateral on a daily basis to ensure that credit exposures are appropriately collateralised. The company seeks to minimise exposures where there is a significant positive correlation between the creditworthiness of counterparties and the market value of collateral received.

When the company does not have sufficient visibility into a counterparty's financial strength or when it believes a counterparty requires support from its parent company, the company may obtain third party guarantees of the counterparty's obligations. The company also mitigates its credit risk using credit derivatives.

Credit exposures (audited)

GSI's credit exposures are described further below.

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

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

STRATEGIC REPORT (continued)

12. Credit risk management (continued)

Debtors. The company is exposed to credit risk from its debtors through its amounts due from brokers / dealers and customers and amounts due from group undertakings. These primarily comprise receivables related to cash collateral paid to counterparties in respect of derivative financial instruments. In addition, these balances also include initial margin placed with clearing organisations, collateralised receivables related to customer securities transactions and receivables related to sales of securities which have traded, but not yet settled. These receivables generally have minimal credit risk due to the low probability of clearing organisation default and the short-term nature of receivables related to securities settlements.

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

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

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

Credit exposure by financial asset class

	31 December 2014					
	Gross exposure US$m	**Assets captured by market risk US$m**	**Master netting agreements US$m**	**Cash collateral US$m**	**Security collateral received US$m**	**Net credit exposure US$m**
Financial asset class:						
Financial instruments owned	667,823	(37,099)	(548,820)	(44,601)	(11,349)	25,954
Financial instruments owned pledged as collateral	24,404	(24,404)	-	-	-	-
Collateralised agreements	219,234	-	(15,595)	-	(201,597)	2,042
Debtors	77,142	-	-	(29,514)	(8,814)	38,814
Cash at bank and in hand	3,586	-	-	-	-	3,586
Total	**992,189**	**(61,503)**	**(564,415)**	**(74,115)**	**(221,760)**	**70,396**

STRATEGIC REPORT (continued)

12. Credit risk management (continued)

	31 December 2013					
	Gross exposure US$m	Assets captured by market risk US$m	Master netting agreements US$m	Cash collateral US$m	Security collateral received US$m	Net credit exposure US$m
Financial asset class:						
Financial instruments owned	489,841	(44,588)	(380,418)	(35,386)	(9,681)	19,768
Financial instruments owned pledged as collateral	26,264	(26,264)	-	-	-	-
Collateralised agreements	225,854	-	(14,378)	-	(209,530)	1,946
Debtors	69,511	-	-	(24,075)	(12,375)	33,061
Cash at bank and in hand	4,032	-	-	-	-	4,032
Total	**815,502**	**(70,852)**	**(394,796)**	**(59,461)**	**(231,586)**	**58,807**

The table below presents the company's gross and net credit exposure to financial assets based on internally determined public rating agency equivalents. The unrated net credit exposure of US$7.0 billion (2013: US$8.2 billion) primarily relates to debtors balances of US$4.8 billion (2013: US$6.7 billion) and financial instruments owned with affiliates of US$1.9 billion (2013: US$1.2 billion) for which the company has not assigned an internally determined public rating agency equivalent.

Credit exposure by credit rating equivalent

	31 December 2014					
	Gross exposure US$m	Assets captured by market risk US$m	Master netting agreements US$m	Cash collateral US$m	Security collateral received US$m	Net credit exposure US$m
Credit rating equivalent:						
AAA/Aaa	8,326	-	(4,024)	(1,800)	(334)	2,168
AA/Aa	129,646	-	(63,939)	(17,696)	(34,298)	13,713
A/A	644,916	-	(428,737)	(29,186)	(157,707)	29,286
BBB/Baa2	95,411	-	(53,360)	(16,551)	(14,128)	11,372
BB/Ba2 or lower	43,923	-	(14,250)	(8,760)	(14,090)	6,823
Unrated	69,967	(61,503)	(105)	(122)	(1,203)	7,034
Total	**992,189**	**(61,503)**	**(564,415)**	**(74,115)**	**(221,760)**	**70,396**

	31 December 2013					
	Gross exposure US$m	Assets captured by market risk US$m	Master netting agreements US$m	Cash collateral US$m	Security collateral received US$m	Net credit exposure US$m
Credit rating equivalent:						
AAA/Aaa	7,842	-	(3,114)	(2,635)	(515)	1,578
AA/Aa	85,563	-	(36,867)	(9,127)	(28,957)	10,612
A/A	521,715	-	(304,958)	(26,703)	(165,636)	24,418
BBB/Baa2	78,212	-	(39,992)	(14,017)	(15,558)	8,645
BB/Ba2 or lower	40,534	-	(9,767)	(6,965)	(18,438)	5,364
Unrated	81,636	(70,852)	(98)	(14)	(2,482)	8,190
Total	**815,502**	**(70,852)**	**(394,796)**	**(59,461)**	**(231,586)**	**58,807**

STRATEGIC REPORT (continued)

12. Credit risk management (continued)

In addition to credit risk on financial assets, the company also has credit exposure in respect of contingent and forward starting resale and securities borrowing agreements. The company's gross credit exposure related to these activities is US$34.6 billion as at 31 December 2014 (2013: US$39.8 billion); however, this will be mitigated by collateral of approximately US$33.8 billion (2013: US$39.5 billion) if these commitments are fulfilled. As a result, the company's net credit exposure to these commitments was US$0.8 billion (2013: US$0.3 billion).

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

13. Operational risk management

Overview (audited)

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Exposure to operational risk arises from routine processing errors as well as extraordinary incidents, such as major systems failures.

Potential types of loss events related to internal and external operational risk include:

- Clients, products and business practices;
- Execution, delivery and process management;
- Business disruption and system failures;
- Employment practices and workplace safety;
- Damage to physical assets;
- Internal fraud; and
- External fraud.

GSI's framework for managing operational risk is fully integrated in GS Group's comprehensive control framework designed to provide a well-controlled environment to minimise operational risks. In GSI, the EMEA Operational Risk Committee provides regional oversight for ongoing development and implementation of the operational risk framework and promotion of a robust overall control environment. Operational Risk Management is a risk management function independent of revenue-producing units, reports to GS Group's chief risk officer and is responsible for developing and implementing policies, methodologies and a formalised framework for operational risk management with the goal of minimising exposure to operational risk.

STRATEGIC REPORT (continued)

13. Operational risk management (continued)

Operational risk management process (audited)

Managing operational risk requires timely and accurate information as well as a strong control culture. Operational risk is managed through:

- The training, supervision and development of people;
- The active participation of senior management in identifying and mitigating key operational risks;
- Independent control and support functions that monitor operational risk on a daily basis, and implementation of extensive policies and procedures, and controls designed to prevent the occurrence of operational risk events;
- Proactive communication between revenue-producing units and independent control and support functions; and
- A network of systems throughout GS Group, including GSI, to facilitate the collection of data used to analyse and assess operational risk exposure.

Top-down and bottom-up approaches are combined to manage and measure operational risk. From a top-down perspective, senior management assesses firmwide and business level operational risk profiles. From a bottom-up perspective, revenue-producing units and independent control and support functions are responsible for risk management on a day-to-day basis, including identifying, mitigating, and escalating operational risks to senior management.

The operational risk framework is in part designed to comply with the operational risk measurement rules under Basel III and has evolved based on the changing needs of the company's businesses and regulatory guidance. The framework comprises the following practices:

- Risk identification and reporting;
- Risk measurement; and
- Risk monitoring.

Internal audit performs an independent review of the operational risk framework, including key controls, processes and applications, on an annual basis to assess the effectiveness of the framework.

Risk identification and reporting

The core of the operational risk management framework is risk identification and reporting. A comprehensive data collection process is in place, including firmwide policies and procedures, for operational risk events.

Policies are in place that require managers in the revenue-producing units and independent control and support functions to escalate operational risk events. When operational risk events are identified, policies require that the events be documented and analysed to determine whether changes are required in the systems and / or processes to further mitigate the risk of future events.

In addition, firmwide systems capture internal operational risk event data, key metrics such as transaction volumes, and statistical information such as performance trends. An internally-developed operational risk management application is used to aggregate and organise this information. Managers from both revenue-producing units and independent control and support functions analyse the information to evaluate operational risk exposures and identify businesses, activities or products with heightened levels of operational risk. Periodic operational risk reports are provided to senior management, the GSI Risk Committee and the GSI board of directors.

STRATEGIC REPORT (continued)

13. Operational risk management (continued)

Risk measurement

GSI's operational risk exposure is measured over a twelve-month time horizon using both statistical modelling and scenario analyses, which involve qualitative assessments of the potential frequency and extent of potential operational risk losses, for each of GSI's businesses. Operational risk measurement incorporates qualitative and quantitative assessments of factors including:

- Internal and external operational risk event data;
- Assessments of GSI's internal controls;
- Evaluations of the complexity of GSI's business activities;
- The degree of and potential for automation in GSI's processes;
- New product information;
- The legal and regulatory environment;
- Changes in the markets for GSI's products and services, including the diversity and sophistication of GSI's customers and counterparties; and
- The liquidity of the capital markets and the reliability of the infrastructure that supports the capital markets.

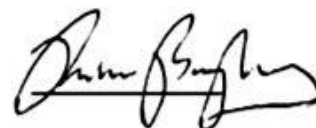
The results from these scenario analyses are used to monitor changes in operational risk and to determine business lines that may have heightened exposure to operational risk. These analyses ultimately are used in the determination of the appropriate level of operational risk capital to hold.

Risk monitoring

Changes in the operational risk profile of GSI, including changes in business mix or jurisdictions in which GSI operates, are evaluated by monitoring the factors noted above at the company level. GSI has both detective and preventive internal controls, which are designed to reduce the frequency and severity of operational risk losses and the probability of operational risk events. The company monitors the results of assessments and independent internal audits of these internal controls.

14. Date of authorisation of issue

The strategic report was authorised for issue by the Board of Directors on 26 March 2015.



BY ORDER OF THE BOARD
A.J. BAGLEY
Secretary
26 March 2015

Part 2: Directors' report and audited financial statements

DIRECTORS' REPORT

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

1. Introduction

In accordance with section 414A of the Companies Act 2006, the directors have prepared a strategic report, which is included in Part 1 of this annual report and which contains a review of the company's businesses and a description of the principal risks and uncertainties facing the company. The directors have chosen to disclose the company's risk management objectives and policies, including exposures to market risk, credit risk and liquidity risk, and the future outlook of the company in the strategic report in accordance with section 414C(11) of the Companies Act 2006.

2. Dividends

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

3. Exchange rate

The British pound / U.S. dollar exchange rate at the balance sheet date was £ / US$ 1.5579 (2013: £ / US$ 1.6567). The average rate for the year was £ / US$ 1.6455 (2013: £ / US$ 1.5670).

4. Employment of disabled persons

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

5. Employee involvement

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

6. Directors

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

Name
P. D. Sutherland, Chairman
R. J. Gnodde, Executive director and co-chief executive officer
M. S. Sherwood, Executive director and co-chief executive officer
C. A. G. Dahlbäck
Lord Griffiths of Fforestfach
R. A. Vince, Executive director and chief operating officer

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

DIRECTORS' REPORT (continued)

7. Disclosure of information to auditors

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

- So far as each of the directors is aware, there is no relevant audit information of which the company's auditors are unaware; and

- Each of the directors has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the company's auditors are aware of that information.

8. Independent auditors

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

9. Charitable contributions

During the year, an amount of US$24,679,541 (2013: US$37,528,225) was donated to charity. Of this amount, US$20,792,819 (2013: US$33,300,000) was donated to Goldman Sachs Gives (UK), a registered charity, for general charitable purposes in England and Wales.

10. Statement of directors' responsibilities

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

- Select suitable accounting policies and then apply them consistently;

- Make judgements and estimates that are reasonable and prudent;

- State whether applicable accounting standards have been followed subject to any material departures disclosed and explained in the financial statements; and

- Prepare the accounts on the going concern basis unless it is inappropriate to presume that the company will continue in business.

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

The directors are responsible for the maintenance and integrity of the company's financial statements on the Goldman Sachs website. Legislation in the U.K. governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

DIRECTORS' REPORT (continued)

11. Date of authorisation of issue

The financial statements were authorised for issue by the Board of Directors on 26 March 2015.

BY ORDER OF THE BOARD
A.J. BAGLEY
Secretary
26 March 2015

Independent auditors' report to the members of
GOLDMAN SACHS INTERNATIONAL
(unlimited company)

Report on the financial statements

Our opinion

In our opinion the financial statements, defined below:

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

This opinion is to be read in the context of what we say in the remainder of this report.

What we have audited

The financial statements, which are prepared by Goldman Sachs International, comprise:

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

Certain required disclosures have been presented elsewhere in the Annual Report, rather than in the notes to the financial statements. These are cross-referenced from the financial statements and are identified as audited.

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

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

Opinion on other matter prescribed by the Companies Act 2006

In our opinion the information given in the Directors' Report and Strategic Report for the financial year for which the financial statements are prepared is consistent with the financial statements.

Other matters on which we are required to report by exception

Adequacy of accounting records and information and explanations received

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

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

We have no exceptions to report arising from this responsibility.

Directors' remuneration

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

Responsibilities for the financial statements and the audit

Our responsibilities and those of the directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 57, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view.

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

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

What an audit of financial statements involves

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

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

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

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

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

Duncan McNab (Senior Statutory Auditor)

For and on behalf of PricewaterhouseCoopers LLP

Chartered Accountants and Statutory Auditors

7 More London Riverside

London

SE1 2RT

26 March 2015

PROFIT AND LOSS ACCOUNT
for the year ended 31 December 2014

	Note	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Net revenue	3	5,898,602	5,156,688
Administrative expenses	4	(3,624,470)	(4,538,515)
OPERATING PROFIT		2,274,132	618,173
Loss on sale of subsidiary undertaking	12	-	(36,238)
Interest payable and similar charges	5	(222,124)	(305,837)
Net finance income	8	28,467	21,468
PROFIT ON ORDINARY ACTIVITIES BEFORE TAXATION		2,080,475	297,566
Tax on profit on ordinary activities	10	(456,004)	(128,902)
PROFIT ON ORDINARY ACTIVITIES AFTER TAXATION AND FOR THE FINANCIAL YEAR	22	1,624,471	168,664

Net revenue and operating profit of the company are derived from continuing operations in the current and prior years.

STATEMENT OF TOTAL RECOGNISED GAINS AND LOSSES
for the year ended 31 December 2014

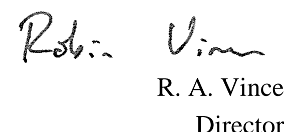
	Note	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Profit for the financial year		1,624,471	168,664
Actuarial gain / (loss) relating to the pension scheme	8	90,173	(70,358)
U.K. deferred tax attributable to the actuarial gain / (loss)	17	(18,035)	8,712
TOTAL RECOGNISED GAINS AND LOSSES RELATING TO THE FINANCIAL YEAR AND SINCE LAST FINANCIAL STATEMENTS		1,696,609	107,018

The notes on pages 64 to 103 form an integral part of these financial statements.
Independent auditors' report – pages 59 to 60.

BALANCE SHEET
as at 31 December 2014

	Note	31 December 2014 US$'000	31 December 2013 US$'000
FIXED ASSETS			
Tangible assets	11	12,216	14,339
Investments	12	1,660	1,198
		13,876	15,537
CURRENT ASSETS			
Financial instruments owned	13	667,823,041	489,841,270
Financial instruments owned pledged as collateral	13	24,404,391	26,263,531
Collateralised agreements	14	219,233,902	225,854,255
Debtors	15	77,642,208	70,211,487
Cash at bank and in hand	26	3,586,142	4,032,081
		992,689,684	816,202,624
CREDITORS: AMOUNTS FALLING DUE WITHIN ONE YEAR			
Financial instruments sold, but not yet purchased	13	(641,404,313)	(457,164,133)
Collateralised financing	16	(157,368,695)	(190,210,848)
Other creditors	18	(155,474,005)	(133,349,677)
		(954,247,013)	(780,724,658)
NET CURRENT ASSETS		38,442,671	35,477,966
TOTAL ASSETS LESS CURRENT LIABILITIES		38,456,547	35,493,503
CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR	19	(16,700,042)	(15,331,681)
PROVISIONS FOR LIABILITIES	20	(16,792)	(17,740)
NET ASSETS EXCLUDING PENSION SURPLUS		21,739,713	20,144,082
Pension surplus	8, 22	257,367	156,389
NET ASSETS INCLUDING PENSION SURPLUS		21,997,080	20,300,471
CAPITAL AND RESERVES			
Called up share capital	21, 22	533,447	533,447
Share premium account	22	2,862,936	2,862,936
Capital reserve (non-distributable)	22	17,286	17,286
Profit and loss account	22	18,583,411	16,886,802
TOTAL SHAREHOLDER'S FUNDS	22	21,997,080	20,300,471

The financial statements were approved by the Board of Directors on 25 March 2015 and signed on its behalf by:



R. A. Vince
Director

The notes on pages 64 to 103 form an integral part of these financial statements.
Independent auditors' report – pages 59 to 60.
Company number: 02263951

STATEMENT OF CASH FLOWS
for the year ended 31 December 2014

	Note	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
NET CASH INFLOW FROM OPERATING ACTIVITIES	24	87,369	4,278,692
RETURNS ON INVESTMENTS AND SERVICING OF FINANCE			
Interest paid		(165,607)	(473,081)
		(165,607)	(473,081)
TAXATION (PAID) / RECEIVED			
Taxation received		14,481	1,575
Taxation paid		(168,945)	(120,280)
		(154,464)	(118,705)
CAPITAL EXPENDITURE AND FINANCIAL INVESTMENTS			
Payments to acquire tangible fixed assets		(2,059)	(1,669)
		(2,059)	(1,669)
ACQUISITIONS AND DISPOSALS			
Acquisition of units in subsidiary undertaking		-	(296,162)
Redemption of units in subsidiary undertaking		-	566,418
		-	270,256
CASH (OUTLFOW) / INFLOW BEFORE USE OF FINANCING		(234,761)	3,955,493
FINANCING			
Receipts from issuing long-term subordinated debt		-	1,950,000
Repayment of long-term subordinated debt		-	(5,000,000)
		-	(3,050,000)
(DECREASE) / INCREASE IN CASH	25, 26	(234,761)	905,493

The notes on pages 64 to 103 form an integral part of these financial statements.

Independent auditors' report – pages 59 to 60.

1. ACCOUNTING POLICIES

a. Accounting convention

The financial statements have been prepared on the going concern basis, under the historical cost convention (modified as explained in *notes 1i* and *1m*), and in accordance with the Companies Act 2006 and applicable accounting standards in the United Kingdom. The principal accounting policies are set out below and have been applied consistently throughout the year.

b. Consolidation

The company has elected not to prepare consolidated financial statements as permitted by section 402 of the Companies Act 2006 as its subsidiaries are not material for the purpose of giving a true and fair view.

c. Revenue recognition

Net revenue has been disclosed instead of turnover as this more meaningfully reflects the nature and results of the company's activities. Net revenue, which is after charging related expenses, includes the net profit arising from transactions in securities, foreign exchange and other financial instruments, and fees and commissions earned. Related expenses include trading interest and dividends payable less trading interest and dividends receivable.

Financial assets and financial liabilities measured at fair value through profit or loss

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

Investment Banking

Fees from financial advisory engagements and underwriting revenues are recognised in profit and loss when the relevant parties are contractually bound and as contract activity progresses unless the right to consideration does not arise until the occurrence of a critical event, in which case revenue is not recognised until that event has occurred.

Expenses associated with such engagements are deferred until the related revenue is recognised or the engagement is otherwise concluded. Expenses associated with financial advisory engagements are recognised in administrative expenses, net of client reimbursements. Underwriting revenues are presented net of related expenses.

Investment Management

Management fees are recognised on an accrual basis and are generally calculated as a percentage of a fund or a separately managed account's average net asset value and are recognised over the period that the related service is provided.

Incentive fees are calculated as a percentage of a fund's return or a percentage of a fund's excess return above a specified benchmark or other performance target. Incentive fees are recognised only when all material contingencies have been resolved.

Commissions and Fees

Revenue from commissions and fees from executing and clearing client transactions on stock, options and futures markets, as well as OTC transactions is recognised in net revenue on the day the trade is executed.

1. ACCOUNTING POLICIES (continued)

d. Operating leases

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

e. Short-term employee benefits

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

f. Share-based payments

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

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

g. Foreign currencies

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

h. Dividends

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

i. Pension costs

The company is a sponsor of a defined contribution pension plan and a hybrid pension plan for the benefit of certain employees. The hybrid pension plan has both a defined benefit section ('the Plan') and a defined contribution section. These are accounted for as follows:

- For the defined contribution pension plan and the defined contribution section of the hybrid pension plan, the contributions payable for the year are charged to operating profit. Differences between contributions payable for the year and contributions actually paid are shown as either accruals or prepayments on the balance sheet.

1. ACCOUNTING POLICIES (continued)

i. Pension cost (continued)

- For the Plan, the amounts charged to operating profit are the current service costs, any past service costs and any gains or losses on settlements and curtailments. They are included as part of staff costs. The interest cost and expected return on assets are shown as a net amount within net finance income. Actuarial gains and losses are recognised immediately in the statement of total recognised gains and losses. The Plan is funded, with the assets of the scheme held separately from those of the company, in separate trustee-administered funds. Plan assets are measured at fair value and Plan liabilities are measured on an actuarial basis using the projected unit method and discounted at a rate equivalent to the current rate of return on a high-quality corporate bond of equivalent currency and term to the scheme liabilities. Full actuarial valuations are obtained at least triennially and updated at each balance sheet date. Any surplus or deficit of Plan assets over Plan liabilities is recognised on the balance sheet as an asset (surplus) or liability (deficit).

j. Tangible fixed assets

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

	Years
Fixtures, fittings and equipment	3-7

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

k. Fixed asset investments

Fixed asset investments are stated at cost or amortised cost, as applicable, less provision for any impairment. Amortisation is included in administrative expenses.

l. Cash at bank and in hand

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

m. Financial instruments

i. Recognition and derecognition

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

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

1. ACCOUNTING POLICIES (continued)

m. Financial instruments (continued)

ii. Classification and measurement

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

Financial instruments classified as held for trading

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

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

Financial instruments designated at fair value through profit or loss

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

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

Hybrid financial instruments are instruments that contain bifurcatable embedded derivatives. If the company elects to bifurcate the embedded derivative from the associated debt, the derivative is accounted for at fair value and the host contract is accounted for at amortised cost, adjusted for the effective portion of any fair value hedges. If the company does not elect to bifurcate, the entire hybrid financial instrument is designated at fair value through profit or loss.

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

- Resale and substantially all repurchase agreements;
- Securities borrowed and loaned within Fixed Income, Currency and Commodities Client Execution;
- Substantially all secured debt securities issued, which includes certain hybrid financial instruments and transfers of assets accounted for as financings rather than sales;
- Certain unsecured debt securities issued, including certain hybrid financial instruments; and
- Certain debtors, including transfers of assets accounted for as secured loans rather than purchases.

1. ACCOUNTING POLICIES (continued)

m. Financial instruments (continued)

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

Loans and receivables; and financial liabilities measured at amortised cost

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

Financial liabilities measured at amortised cost include certain collateralised financing and substantially all other creditors. Such financial liabilities are initially recognised at fair value plus transactions costs and subsequently measured at amortised cost using the effective interest method (see below). Finance costs, including discounts allowed on issue, are recorded in net revenue with the exception of interest on long-term subordinated loans, which is recorded in interest payable and similar charges.

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

The company assesses its loans and receivables at each balance sheet date for any objective evidence of impairment. If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the financial asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The amount of the loss is included within net revenue, if trading related, or in administrative expenses if non-trading related.

iii. Classification of financial liabilities and equity

Financial liabilities and equity instruments are classified according to the substance of the contractual arrangements. An equity investment is any contract that evidences a residual interest in the assets of the entity after deducting all liabilities. Instruments are evaluated to determine if they contain both liability and equity components. The initial carrying amount of a compound financial instrument is allocated first to the liability component, measured at fair value, and the equity is assigned the residual amount.

iv. Offsetting financial assets and financial liabilities

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

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

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

1. ACCOUNTING POLICIES (continued)

m. Financial instruments (continued)

v. Fair value measurements

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

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

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

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

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

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

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

<u>Cash instruments</u>

Cash instruments include government and agency obligations, bank loans and bridge loans, corporate debt securities, equities and convertible debentures, and other non-derivative financial instruments owned and financial instruments sold, but not yet purchased. Valuation techniques and significant inputs for each level of the fair value hierarchy include:

- Level 1 cash instruments that are valued using quoted prices for identical unrestricted instruments in active markets.

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

1. ACCOUNTING POLICIES (continued)

m. Financial instruments (continued)

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

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

Derivatives

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

- Level 1 derivatives include short-term contracts for future delivery of securities when the underlying security is a level 1 instrument, and exchange-traded derivatives if they are actively traded and are valued at their quoted market price.

- Level 2 derivatives include OTC derivatives for which all significant valuation inputs are corroborated by market evidence and exchange-traded derivatives that are not actively traded and / or that are valued using models that calibrate to market-clearing levels of OTC derivatives. In evaluating the significance of a valuation input, the company considers, among other factors, a portfolio’s net risk exposure to that input.

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

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

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

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

1. ACCOUNTING POLICIES (continued)

m. Financial instruments (continued)

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

vi. Hedge accounting

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

n. Collateralised agreements and financing

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

o. Current and deferred taxation

The tax expense for the period comprises current and deferred taxation. Tax is recognised in the profit and loss account, except to the extent it relates to items recognised in the statement of total recognised gains and losses.

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

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

- Deferred tax assets are recognised only to the extent that the directors consider that it is more likely than not that there will be suitable taxable profits from which the future reversal of the underlying timing differences can be deducted.

- Deferred tax is measured on an undiscounted basis at the tax rates that are expected to apply in the periods in which timing differences reverse, based on tax rates and laws enacted or substantively enacted at the balance sheet date.

Deferred tax is recognised in the profit and loss account or directly in the statement of total recognised gains and losses according to where the associated gain or loss, to which the deferred tax is attributable, is recognised.

1. ACCOUNTING POLICIES (continued)

p. Provisions and contingent liabilities

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

Contingent liabilities are:

- Possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events outside the control of the company; or
- Present obligations that have arisen from past events but which are not recognised because either an outflow of economic benefits is not probable or the amount of the obligations cannot be reliably measured.

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

2. REPORTING AND DISCLOSURE EXEMPTIONS

a. FRS8 'Related Party Disclosures'

The company is a wholly-owned subsidiary of Group Inc. whose consolidated financial statements include the company and are publicly available. As a result, under the terms of paragraph 3(c) of FRS8, 'Related Party Disclosures', the company is exempt from disclosing transactions with companies also wholly owned within The Goldman Sachs Group, Inc.

3. NET REVENUE

The company's net revenue is categorised into the following business segments:

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Investment Banking	1,379,681	1,097,931
Institutional Client Services	3,762,428	3,715,380
Investing & Lending[1]	266,853	14,740
Investment Management[1]	489,640	328,637
	5,898,602	**5,156,688**

1. The company has reclassified US$150 million of net revenue for 2013 from Investing & Lending to Investment Management associated with providing investing services to funds managed by GS Group. There is no impact to total net revenue.

In addition to transactions entered into with third parties, the company also enters into transactions with affiliates in the normal course of business as part of market-making activities and general operations. Revenues are allocated to, and received from, such affiliates for these transactions.

Net revenue in the above business segments includes interest income and interest expense on cash instruments, collateralised arrangements, and other positions in relation to the cash generated by, or funding requirements of, such underlying positions with the exception of interest on long-term subordinated loans, which is presented in interest payable and similar charges (see *note 5 to the financial statements*).

3. NET REVENUE (continued)

Refer to *Item 5 (Results of operations – Segment reporting)* in Part 1 of this annual report for a description and analysis of the company's segments.

Net revenue includes net interest income of US$415 million (2013: US$106 million) and non-interest income of US$5.5 billion (2013: US$5.1 billion).

Net interest income includes interest income of US$2.5 billion (2013: US$2.6 billion) and interest expense of US$2.1 billion (2013: US$2.5 billion). Of interest income, US$22 million (2013: US$147 million) relates to parent and group undertakings and of interest expense, US$852 million (2013: US$959 million) relates to parent and group undertakings.

Non-interest income includes commissions and fees income of US$657 million for 2014 (2013: US$596 million), which is included within the Institutional Client Services and Investment Management segments. Net revenue in Institutional Client Services includes net losses of US$489 million (2013: US$84 million) in relation to the company's financial assets and financial liabilities designated at fair value. The remaining net revenue within Institutional Client Services predominately relates to net gains from financial assets and financial liabilities held for trading.

Geographical Analysis

Due to the highly integrated nature of international financial markets, the directors consider that the company operates in a single global market. As a result, no disclosure of segmental information relating to the geographical origin of results has been provided.

4. ADMINISTRATIVE EXPENSES

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Direct costs of employment (see note 7)	3,042,037	3,800,742
Market development	100,007	95,769
Communications and technology	84,812	80,845
Depreciation of tangible fixed assets (see note 11)	3,660	3,394
Occupancy (see note a)	180,472	166,665
Professional fees (see note b)	119,833	110,136
Other expenses (see note c)	93,649	280,964
	3,624,470	**4,538,515**

a. Occupancy expenses include operating lease rentals for land and buildings of US$87 million (2013: US$84 million).

b. Professional fees include fees payable of US$5.3 million (2013: US$5.0 million) to the company's auditors for the audit of the company's annual accounts and fees payable of US$0.6 million (2013: US$0.4 million) to the company's auditors for other services.

c. Other expenses include miscellaneous taxes, charitable contributions, management fees charged by and to group undertakings relating to operational and administrative support, management services received from and provided to affiliates and losses on disposal of tangible fixed assets of US$522 thousand (2013: US$nil).

5. INTEREST PAYABLE AND SIMILAR CHARGES

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Payable to group undertakings	**222,124**	**305,837**

Interest payable and similar charges payable to group undertakings arise on long-term subordinated loans (see note 19a).

6. DIRECTORS' EMOLUMENTS

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Aggregate emoluments	5,856	4,737
Company pension contributions to money purchase schemes	7	7
	5,863	**4,744**

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Highest paid director:		
Aggregate emoluments and benefits	1,930	1,400
Company pension contributions to money purchase schemes	3	3
Accrued annual pension at end of year	8	7

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

One director is a member of a defined contribution pension plan and one director is a member of the hybrid pension plan (including the defined benefit section and defined contribution section). Four directors, including the highest paid director, have been granted Group Inc. shares in respect of long-term incentive schemes during the year. Two directors, including the highest paid director, have exercised options during the year.

7. STAFF COSTS

The average number of staff (employees including directors, and consultants and temporary staff) is analysed below:

	Year Ended 31 December 2014 Number	Year Ended 31 December 2013 Number
Employees including directors:		
Investment Banking	696	674
Institutional Client Services	1,400	1,388
Investing & Lending	111	98
Investment Management	534	503
Support Functions	2,503	2,479
	5,244	**5,142**
Consultants and temporary staff	**338**	**320**
	5,582	**5,462**

7. STAFF COSTS (continued)

The company has the use of a number of individuals who are employed by affiliated entities and seconded to the company. These seconded individuals are included in the disclosure of headcount and related staff costs. Consultants and temporary staff costs are included in total direct costs of employment, below. Total headcount as at 31 December 2014 was 5,730 (2013: 5,555).

The employment costs incurred by the company, including those relating to directors, were:

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Aggregate gross wages and salaries	2,621,155	3,331,710
Employer's National Insurance Contributions	314,384	373,016
Pension costs, employer contributions to the:		
Defined contribution plan and defined contribution section of the hybrid pension plan	60,753	55,587
Defined benefit section of the hybrid pension plan	45,745	40,429
Total direct costs of employment	**3,042,037**	**3,800,742**

Total direct costs of employment include a charge of US$83 million (2013: charge of US$1.0 billion) relating to the mark-to-market of share-based compensation.

8. PENSION ARRANGEMENTS

The company sponsors an open pension plan with a hybrid structure, having both a defined benefit section ('the Plan') and a defined contribution section. The Plan was closed to new entrants with effect from 1 April 2008 and was replaced by a defined contribution plan. The Plan allows existing participants to continue to accrue benefits. In 2014, the company notified plan participants that it intends to close the Plan to future benefit accruals after 31 March 2016.

A full actuarial valuation of the Plan was carried out by a qualified independent actuary as at 31 December 2012 using the projected unit funding method and updated to 31 December 2014.

The major financial assumptions used by the actuary underlying the funding of the Plan which had the most significant effect on the pension cost are set out below:

	Year Ended 31 December 2014 *% per annum*	Year Ended 31 December 2013 *% per annum*
Discount rate	3.80	4.50
Rate of increase in salaries	4.00	4.00
Rate of increase in pensions in payment (post-30 November 1996 accrual)	3.10	3.40
Rate of increase in pensions in deferment (post-30 November 1996 accrual)	2.30	2.60
Rate of price inflation	3.30	3.60

8. PENSION ARRANGEMENTS (continued)

The assets in the Plan attributable to the company and the expected rates of return were:

	31 December 2014		31 December 2013	
	Expected rate of return *% per annum*	Market value US$m	Expected rate of return *% per annum*	Market value US$m
Equities	6.8	991.6	7.1	969.1
Bonds	2.5	707.3	4.0	404.9
Cash and reinvested cash	2.7	118.1	2.9	134.7
Total market value of assets		**1,817.0**		**1,508.7**

Development of the balance sheet:

	31 December 2014 US$m	31 December 2013 US$m	31 December 2012 US$m	31 December 2011 US$m	31 December 2010 US$m
Market value of Plan assets	1,817.0	1,508.7	1,266.6	1,059.6	1,053.6
Actuarial value of Plan liabilities	1,559.6	1,352.3	1,054.1	927.4	889.6
Surplus in the Plan and pension asset recognised in the balance sheet before deferred taxation	**257.4**	**156.4**	**212.5**	**132.2**	**164.0**

The defined benefit cost was formed of the following components:

	Year Ended 31 December 2014 US$m	Year Ended 31 December 2013 US$m
Analysis of amounts charged to operating profit:		
Current service cost	45.7	40.4
Total charged to operating profit	**45.7**	**40.4**
Analysis of the amount credited to net finance income:		
Interest on Plan liabilities	60.2	49.6
Expected return on assets in the Plan	(88.7)	(71.1)
Total credited to net finance income	**(28.5)**	**(21.5)**
Total charged to profit and loss before tax	**17.2**	**18.9**
Analysis of amounts recognised in the statement of total recognised gains and losses:		
Actual less expected gain on assets	297.8	111.1
Experience gain on liabilities	19.1	11.0
Loss on change in assumptions (financial and demographic)	(226.7)	(192.5)
Total gain / (loss) recognised in the statement of total recognised gains and losses before tax	**90.2**	**(70.4)**

8. PENSION ARRANGEMENTS (continued)

History of experience gains and losses are as follows:

	31 December 2014	31 December 2013	31 December 2012	31 December 2011	31 December 2010
Actual less expected gain / (loss) on Plan assets:					
Amount (US$m)	297.8	111.1	57.2	(101.1)	14.0
% of Plan assets at end of the year	16.4%	7.4%	4.5%	9.5%	1.3%
Experience gain on Plan liabilities:					
Amount (US$m)	19.1	11.0	17.5	28.5	48.6
% of Plan liabilities at end of the year	1.2%	0.8%	1.7%	3.1%	5.5%
Total actuarial gain / (loss) recognised in statement of total recognised gains and losses:					
Amount (US$m)	90.2	(70.4)	60.4	(51.9)	88.2
% of Plan liabilities at end of the year	5.8%	5.2%	5.7%	5.6%	9.9%

Analysis of the movement in Plan assets during the year:

	Year Ended 31 December 2014 US$m	Year Ended 31 December 2013 US$m
Plan assets at the start of the year	1,508.7	1,266.6
Expected return on Plan assets	88.7	71.1
Actual less expected gain on assets	297.8	111.1
Contributions paid – Employer	43.6	32.3
Benefits paid	(9.4)	(9.2)
Foreign exchange (losses) / gains on translation of Plan assets	(112.4)	36.8
Plan assets at the end of the year	**1,817.0**	**1,508.7**

Analysis of the movement in Plan liabilities during the year:

	Year Ended 31 December 2014 US$m	Year Ended 31 December 2013 US$m
Plan liabilities at the start of the year	1,352.3	1,054.1
Current service cost	45.7	40.4
Interest on Plan liabilities	60.2	49.6
Loss on change in assumptions	226.7	192.5
Experience gain on liabilities	(19.1)	(11.0)
Benefits paid	(9.4)	(9.2)
Foreign exchange (gains) / losses on translation of Plan liabilities	(96.8)	35.9
Plan liabilities at the end of the year	**1,559.6**	**1,352.3**

8. PENSION ARRANGEMENTS (continued)

Analysis of the movement in surplus in the Plan during the year:

	Year Ended 31 December 2014 US$m	Year Ended 31 December 2013 US$m
Surplus in the Plan at the start of the year	156.4	212.5
Contributions paid – Employer	43.6	32.3
Current service cost	(45.7)	(40.4)
Net finance income	28.5	21.5
Actuarial gain / (loss)	90.2	(70.4)
Foreign exchange (losses) / gains on translation of surplus	(15.6)	0.9
Surplus in the Plan at the end of the year	**257.4**	**156.4**

Additional disclosures:

	Year Ended 31 December 2014 US$m	Year Ended 31 December 2013 US$m
Expected future benefit payments for the year to 31 December 2015 / 31 December 2014	11.4	11.8
Expected contributions for the year to 31 December 2015 / 31 December 2014 – Employer	40.9	41.9
Actual return on Plan assets during the year ended 31 December 2014 / 31 December 2013		
Expected return on Plan assets	88.7	71.1
Actual less expected gain on assets	297.8	111.1
Actual return on Plan assets	**386.5**	**182.2**

Cumulative amounts recognised in the statement of total recognised gains and losses since the adoption of FRS17 Retirement Benefits:

	31 December 2014 US$m	31 December 2013 US$m
Actuarial loss relating to the pension scheme	(11.1)	(101.3)
U.K. deferred tax attributable to the actuarial loss	2.2	20.2
Net cumulative amount recognised in the statement of total recognised gains and losses	**(8.9)**	**(81.1)**

9. SHARE-BASED PAYMENTS

Stock incentive plan

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

GSI recorded share-based compensation in respect of the amortisation of granted equity awards, net of forfeitures, of US$529 million for 2014 (2013: US$525 million). The corresponding credit to equity has been transferred to liabilities as a result of the terms of the intercompany agreements with Group Inc.

Restricted stock units

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

	31 December 2014 No. of RSUs		31 December 2013 No. of RSUs	
	No future service requirement	Future service requirement	No future service requirement	Future service requirement
Outstanding at the beginning of the year	4,237,913	2,214,358	5,000,853	2,533,081
Granted	2,267,175	1,307,601	2,949,686	1,741,276
Forfeited	(77,373)	(288,394)	(35,652)	(219,059)
Delivered	(3,817,768)	-	(5,505,642)	-
Transferred in / (out)	18,953	28,640	7,171	(19,443)
Vested	1,463,485	(1,463,485)	1,821,497	(1,821,497)
Outstanding at the end of the year	**4,092,385**	**1,798,720**	**4,237,913**	**2,214,358**

The weighted average grant-date fair value of RSUs granted during 2014 was US$153.80 (2013: US$126.38). The fair value of the RSUs granted during the year ended 31 December 2014 and the year ended 31 December 2013 includes a liquidity discount of 12.5% and 11.6%, respectively, to reflect post-vesting transfer restrictions of up to 4 years.

In the first quarter of 2015, Group Inc. granted 3.7 million year-end RSUs to the company's employees, of which 0.8 million RSUs require future service as a condition of delivery. These awards are subject to additional conditions as outlined in the award agreements. Generally, shares underlying these awards, net of required withholding tax, deliver over a three-year period but are subject to post-vesting transfer restrictions through January 2020. These grants are not included in the above table.

9. SHARE-BASED PAYMENTS (continued)

Stock options

Stock options granted to employees generally vest as outlined in the applicable stock option agreement. No options have been granted since 2010. In general, options expire on the tenth anniversary of the grant date, although they may be subject to earlier termination or cancellation under certain circumstances in accordance with the terms of the applicable stock option agreement and The Goldman Sachs Amended and Restated Stock Incentive Plan in effect at the time of grant. The table below presents the activity related to stock options.

	31 December 2014		31 December 2013	
	No. of stock options	Weighted average exercise price (US$)	No. of stock options	Weighted average exercise price (US$)
Outstanding at the beginning of the year	10,214,739	90.53	10,256,821	90.55
Exercised	(5,712,248)	78.94	(41,542)	96.08
Expired	-	-	(540)	96.08
Outstanding at the end of the year	**4,502,491**	**105.23**	**10,214,739**	**90.53**
Exercisable at the end of the year	**4,502,491**	**105.23**	**10,214,739**	**90.53**

For those options exercised during the year, the weighted average share price at the date of exercise was US$169.82 (2013: US$153.08). The table below presents options outstanding.

	31 December 2014		31 December 2013	
	No. of stock options outstanding	Weighted average remaining contractual life (years)	No. of stock options outstanding	Weighted average remaining contractual life (years)
Exercise Price				
$75.00-$89.99	3,383,700	4.00	9,078,709	5.00
$90.00-$119.99	-	-	-	-
$120.00-$134.99	271,481	0.92	288,720	1.92
$135.00-$194.99	-	-	-	-
$195.00-$209.99	847,310	2.51	847,310	3.51
Outstanding at the end of the year	**4,502,491**		**10,214,739**	

10. TAX ON PROFIT ON ORDINARY ACTIVITIES

a. Analysis of tax charge for the year:

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Current tax:		
U.K. corporation tax	243,315	151,241
Adjustments in respect of prior periods	39,264	2,275
Overseas taxation	61,980	59,153
Total current tax (see note 10b)	**344,559**	**212,669**
Deferred tax:		
Provisions and other timing differences	104,801	(117,580)
Effect of decreased tax rate on opening asset	-	38,317
Adjustments in respect of prior periods	6,644	(4,504)
Total deferred tax (see note 17)	**111,445**	**(83,767)**
Tax on profit on ordinary activities	**456,004**	**128,902**

b. Factors affecting tax charge for the year:

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

	Year Ended 31 December 2014 US$'000	Year Ended 31 December 2013 US$'000
Profit on ordinary activities before taxation	2,080,475	297,566
Profit on ordinary activities multiplied by standard rate in the U.K. 21.5% (2013: 23.25%)	447,302	69,184
Timing differences in respect of share-based compensation	(93,503)	178,608
Timing differences in respect of pension contribution deduction	(6,534)	(1,831)
Accelerated capital allowances and other timing differences	3,064	(10,529)
Permanent differences	(23,798)	(29,230)
Expenses not deductible for tax purposes	2,501	30,764
Tax losses surrendered from group undertakings for nil consideration	(29,101)	(30,018)
Effect of higher taxes on overseas earnings	11,894	4,441
Exchange differences and other	(6,530)	(995)
Adjustments in respect of prior periods	39,264	2,275
Total current tax	**344,559**	**212,669**

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

11. TANGIBLE FIXED ASSETS

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

	Leasehold improvements US$'000	Fixtures, fittings and equipment US$'000	Total US$'000
Cost			
At 1 January 2014	25,000	7,921	32,921
Additions	361	1,698	2,059
Disposals	(776)	(17)	(793)
At 31 December 2014	**24,585**	**9,602**	**34,187**
Accumulated depreciation			
At 1 January 2014	14,211	4,371	18,582
Charge for the year (see note 4)	2,692	968	3,660
Disposals	(254)	(17)	(271)
At 31 December 2014	**16,649**	**5,322**	**21,971**
Net book value			
At 31 December 2014	**7,936**	**4,280**	**12,216**
At 31 December 2013	**10,789**	**3,550**	**14,339**

12. FIXED ASSET INVESTMENTS

	Shares in subsidiary undertakings US$'000	Other investments, other than loans US$'000	Total US$'000
Cost			
At 1 January 2014	-	1,267	1,267
Additions	-	462	462
At 31 December 2014	**-**	**1,729**	**1,729**
Accumulated amortisation			
At 1 January 2014	-	69	69
Charge for the year	-	-	-
At 31 December 2014	**-**	**69**	**69**
Net book value			
At 31 December 2014	-	**1,660**	**1,660**
At 31 December 2013	-	**1,198**	**1,198**

Other investments, other than loans consists of exchange memberships. The directors consider that the fair value of investments in subsidiary undertakings and other investments, other than loans is not less than their book value.

12. FIXED ASSET INVESTMENTS (continued)

The subsidiaries over which the company exercises control at the year end are listed below:

Name of company	Country of incorporation	Holding and proportion of voting rights	Class shares held	Number held	Nature of business
Goldman Sachs (Cayman) Limited	Cayman Islands	100%	Ordinary shares	250	Financial services
Ipopema 80 Fundusz Inwestycyjny Zamkniety	Poland	100%	*	*	Investment fund

* This subsidiary undertaking is included in the financial statements on the basis of control obtained other than through voting rights attached to shares.

During 2014, the company sold 2 ordinary shares of US$1 each, being the entire share capital issued by Goldman Sachs International Investments Limited, to Goldman Sachs Group UK Limited (‘GSGUK’), the company’s immediate parent undertaking, for a total consideration of US$2 effective 29 August 2014.

In the prior year, the company acquired additional units for BRL595 million (US$296 million) and redeemed units for BRL1.2 billion (US$569 million) in Sphere Fundo De Investimento Multimercado – Investimento No Exterior Credito Privado (‘Sphere Fundo’). The company then transferred its remaining units in Sphere Fundo to GSGUK, the company’s immediate parent undertaking. The consideration of US$191 million was satisfied by way of a short-term loan. The company realised a net loss of US$36 million over the life of this investment due to the weakening of Brazilian real against U.S. dollar. During 2014, the short-term loan of US$191 million was fully repaid to the company.

The company has interests in a number of special purpose vehicles and capital-guaranteed funds which do not meet the definition of a legal subsidiary, but give rise to the risks and rewards that are, in substance, no different than if they were legal subsidiaries. The activities of these special purpose vehicles and the capital-guaranteed funds consist of the issuance of loan notes under the terms of a repackaging programme. These vehicles are consolidated in the financial statements of GSGUK.

13. FINANCIAL INSTRUMENTS OWNED AND FINANCIAL INSTRUMENTS SOLD, BUT NOT YET PURCHASED

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

13. FINANCIAL INSTRUMENTS OWNED AND FINANCIAL INSTRUMENTS SOLD, BUT NOT YET PURCHASED (continued)

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

	31 December 2014 US$'000	31 December 2013 US$'000
Cash instruments[1]:		
Commercial paper, certificates of deposit, time deposits and other money market instruments	1,225,282	3,391,803
Government and agency obligations	16,920,118	20,892,333
Mortgage and other asset-backed loans and securities	1,998,385	2,170,894
Bank loans and bridge loans	1,693,905	556,233
Corporate and other debt obligations	12,217,297	11,440,795
Equities and convertible debentures	30,675,005	34,740,279
	64,729,992	**73,192,337**
Derivative instruments[1]:		
Interest rates	367,155,116	236,325,613
Credit	64,636,465	76,662,753
Currencies	112,717,413	57,229,166
Commodities	15,964,183	5,446,429
Equities	67,024,263	67,248,503
	627,497,440	**442,912,464**
	692,227,432	**516,104,801**
Financial instruments owned	667,823,041	489,841,270
Financial instruments owned pledged as collateral	24,404,391	26,263,531
	692,227,432	**516,104,801**

Financial instruments sold, but not yet purchased comprises:

	31 December 2014 US$'000	31 December 2013 US$'000
Cash instruments:		
Government and agency obligations	10,735,033	10,325,775
Corporate and other debt obligations	2,279,658	2,663,618
Equities and convertible debentures	14,626,885	13,775,194
	27,641,576	**26,764,587**
Derivative instruments:		
Interest rates	359,427,770	231,757,981
Credit	59,747,636	70,760,557
Currencies	113,264,254	57,063,641
Commodities	15,892,208	5,403,872
Equities	65,430,869	65,413,495
	613,762,737	**430,399,546**
	641,404,313	**457,164,133**

1. The company has reclassified US$2.3 billion of financial instruments from derivative instruments to cash instruments and presented cash instruments in more categories as at 31 December 2013. There is no impact to total financial instruments owned, including financial instruments owned pledged as collateral.

14. COLLATERALISED AGREEMENTS

	31 December 2014 US$'000	31 December 2013 US$'000
Resale agreements	131,734,812	136,100,718
Securities borrowed	87,499,090	89,753,537
	219,233,902	**225,854,255**

Of collateralised agreements, US$136.9 billion (2013: US$133.3 billion) relates to group undertakings.

15. DEBTORS

	31 December 2014 US$'000	31 December 2013 US$'000
Amounts due from broker / dealers and customers	63,403,728	54,460,372
Amounts due from parent and group undertakings	13,710,892	15,025,954
Deferred tax (see note 17)	453,676	583,535
Other debtors	34,529	44,250
Prepayments and accrued income	39,383	22,221
Corporation tax receivable	-	75,155
	77,642,208	**70,211,487**

Debtors includes US$77.1 billion (2013: US$69.5 billion) of financial assets and US$500 million (2013: US$701 million) of non-financial assets.

Of the amounts due from broker / dealers and customers, US$981 million (2013: US$180 million) is due in more than one year. These balances relate to secured lending and / or prepaid commodity contracts.

The remaining debtors are all due within one year of the balance sheet date.

16. COLLATERALISED FINANCING

	31 December 2014 US$'000	31 December 2013 US$'000
Repurchase agreements	62,395,909	104,989,680
Securities loaned	94,972,786	85,221,168
	157,368,695	**190,210,848**

Of collateralised financing, US$105.1 billion (2013: US$101.0 billion) relates to group undertakings.

17. DEFERRED TAX

	31 December 2014 US$'000	31 December 2013 US$'000
Deferred tax balance comprises (see note 15):		
Depreciation in excess of capital allowances	3,036	2,960
Post-retirement benefits	(51,473)	(31,278)
Other timing differences	502,113	611,853
	453,676	**583,535**

	US$'000
The movements in the deferred tax balance were as follows:	
At 1 January 2014	583,535
Transfer to the profit and loss account for the year (see note 10a)	(111,445)
Transfer to the statement of total recognised gains and losses for the year	(18,035)
Foreign exchange losses	(379)
At 31 December 2014	**453,676**

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

18. OTHER CREDITORS

Other creditors, all of which are payable within one year of the balance sheet date, comprise:

	31 December 2014 US$'000	31 December 2013 US$'000
Bank loans	110,509	42,560
Overdrafts (see note 26)	8,637	28,245
Debt securities issued (see note a)	15,544,508	18,960,736
Amounts due to broker / dealers and customers	67,073,244	58,457,370
Amounts due to parent and group undertakings – unsecured borrowings	49,463,853	37,856,952
Amounts due to parent and group undertakings – other unsecured creditors	20,992,555	15,273,841
Accrual for management charges payable to parent and group undertakings (see note 19d)	1,076,675	1,523,525
Corporation tax payable	78,033	-
Other taxes and social security costs	250,466	234,419
Other creditors and accruals	875,525	972,029
	155,474,005	**133,349,677**

Other creditors includes US$155.1 billion (2013: US$133.1 billion) of financial liabilities and US$328 million (2013: US$234 million) of non-financial liabilities.

18. OTHER CREDITORS (continued)

a. The classification of short-term debt securities is as follows:

	31 December 2014 US$'000	31 December 2013 US$'000
Unsecured debt securities with affiliates	3,807,021	3,819,734
Unsecured debt securities with external counterparties	9,135,409	8,417,081
Secured debt securities with affiliates	671,961	437,242
Secured debt securities with external counterparties	1,930,117	6,286,679
	15,544,508	**18,960,736**

Secured debt securities are secured by securities which have been pledged as collateral. This pledged collateral is either recognised within financial instruments owned or sourced through collateralised agreements.

19. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR

	31 December 2014 US$'000	31 December 2013 US$'000
Long-term subordinated loans (see note a)	6,458,000	6,458,000
Debt securities issued (see note b)	6,386,954	4,205,847
Amounts due to parent and group undertakings – unsecured borrowings (see note c)	2,702,345	3,549,630
Amounts due to parent and group undertakings – other unsecured creditors	378,547	-
Accrual for management charges payable to parent and group undertakings (see note d)	774,196	1,118,204
	16,700,042	**15,331,681**

As at 31 December 2014 and 31 December 2013, all 'creditors: amounts falling due after more than one year' are financial liabilities.

a. The amounts outstanding at 31 December 2014 and 31 December 2013 are comprised of long-term subordinated loans from group undertakings. The loans are unsecured and carry interest at a margin over the U.S. Federal Reserve's federal funds rate. The margin is reset on a periodic basis to reflect changes in the GS Group's weighted average cost of debt. Long-term subordinated loans of US$6.5 billion (2013: US$6.5 billion) constitute regulatory capital as approved by the PRA and are repayable subject to PRA approval and upon giving or receiving at least 5 years' notice to or from the group undertakings.

19. CREDITORS: AMOUNTS FALLING DUE AFTER MORE THAN ONE YEAR (continued)

b. The classification of long-term debt securities is as follows:

	31 December 2014 US$'000	31 December 2013 US$'000
Unsecured debt securities with affiliates	471,317	101,325
Unsecured debt securities with external counterparties	3,076,081	2,054,357
Secured debt securities with affiliates	1,189,828	545,494
Secured debt securities with external counterparties	1,649,728	1,504,671
	6,386,954	**4,205,847**

Secured debt securities are secured by securities which have been pledged as collateral. This pledged collateral is either recognised within financial instruments owned or sourced through collateralised agreements.

The maturity of debt securities issued due after more than one year is as follows:

	31 December 2014 US$'000	31 December 2013 US$'000
In more than one year, but not more than two years	1,636,681	967,877
In more than two years, but not more than five years	3,058,997	1,990,917
In more than five years	1,691,276	1,247,053
	6,386,954	**4,205,847**

Amounts due in more than five years predominantly relate to structured debt securities with maturities falling from 2020 to 2040. Payments on these securities are typically referenced to underlying financial assets, which are predominately interest rate-related.

c. Amounts due to parent and group undertakings relate to long-term unsecured borrowings from affiliates. As at 31 December 2014, this includes a single loan with a maturity greater than five years of US$400 million (2013: US$400 million) advanced by Restamove Ireland Limited, a fellow group undertaking, under the terms of an uncommitted loan facility dated 26 June 2012. The facility is unsecured, carries interest at a variable rate and has a maturity of 1 July 2022.

d. The accrual for management charges (per above and note 18) is in respect of share-based compensation.

20. PROVISIONS FOR LIABILITIES

	US$'000
At 1 January 2014	17,740
Charge to the profit and loss account	10,000
Reduction in provision	(10,000)
Foreign exchange gain	(948)
At 31 December 2014	**16,792**

The remaining provisions of US$17 million are in respect of legal claims made against the company. Further details relating to the provisions have not been disclosed as permitted by accounting standard FRS12, 'Provisions, Contingent Liabilities and Contingent Assets', on the grounds that it would be seriously prejudicial to do so.

21. SHARE CAPITAL

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

	31 December 2014		31 December 2013	
	No.	US$'000	No.	US$'000
Allotted, called up and fully paid				
Ordinary shares of US$1 each	533,447,150	533,447	533,447,150	533,447
		533,447		**533,447**

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

	Called up share capital US$'000	Share premium account US$'000	Capital reserve (non-distributable) US$'000	Profit and loss account US$'000	Total shareholder's funds US$'000
At 1 January 2013	**533,447**	**2,862,936**	**17,286**	**16,779,784**	**20,193,453**
Profit for the financial year	-	-	-	168,664	168,664
Other recognised losses for the year	-	-	-	(61,646)	(61,646)
Share-based payments (see note 9)	-	-	-	524,935	524,935
Management recharge related to share-based payments	-	-	-	(524,935)	(524,935)
At 1 January 2014	**533,447**	**2,862,936**	**17,286**	**16,886,802**	**20,300,471**
Profit for the financial year	-	-	-	1,624,471	1,624,471
Other recognised gains for the year	-	-	-	72,138	72,138
Share-based payments (see note 9)	-	-	-	528,918	528,918
Management recharge related to share-based payments	-	-	-	(528,918)	(528,918)
At 31 December 2014	**533,447**	**2,862,936**	**17,286**	**18,583,411**	**21,997,080**

Pension reserve

	31 December 2014 US$'000	31 December 2013 US$'000
Profit and loss account excluding pension surplus	18,326,044	16,730,413
Pension surplus (see note 8)	257,367	156,389
Profit and loss account	**18,583,411**	**16,886,802**

23. DIVIDENDS PAID

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

24. RECONCILIATION OF OPERATING PROFIT TO NET CASH INFLOW FROM OPERATING ACTIVITIES

	31 December 2014 US$'000	31 December 2013 US$'000
Operating profit	2,274,132	618,173
Depreciation charges (see notes 4 and 11)	3,660	3,394
Loss on sale of fixed assets (see note 4)	522	-
Withholding taxes related to the redemption of units in subsidiary undertaking	-	2,133
Pension charge net of cash contributions	2,139	8,148
Adjustment for foreign exchange losses / (gains)	207,606	(189,192)
Increase in debtors	(7,657,549)	(7,169,552)
Increase / (decrease) in other creditors	21,993,697	(4,181,309)
Increase in creditors: amounts falling due after more than one year	1,368,361	3,413,093
(Decrease) / increase provisions for liabilities	(948)	2,435
Decrease / (increase) in collateralised agreements	6,620,353	(4,326,700)
(Decrease) / increase in collateralised financing	(32,842,153)	8,733,465
(Increase) / decrease in financial instruments owned, including financial instruments owned pledged as collateral	(176,122,631)	70,374,922
Increase / (decrease) in financial instruments sold, but not yet purchased	184,240,180	(63,010,318)
Net cash inflow from operating activities	**87,369**	**4,278,692**

25. RECONCILIATION OF NET CASH FLOW TO MOVEMENT IN NET DEBT

	31 December 2014 US$'000	31 December 2013 US$'000
Net cash at the start of the year	4,003,836	12,777,368
(Decrease) / increase in cash	(234,761)	905,493
Client money adjustment (see note a)	-	(9,867,224)
Foreign exchange rate changes	(191,570)	188,199
Total cash (see note 26)	**3,577,505**	**4,003,836**
Opening borrowings	(6,458,000)	(9,508,000)
Net decrease in long-term subordinated loans	-	3,050,000
Closing borrowings (see note 19)	**(6,458,000)**	**(6,458,000)**
Net debt (see note 26)	**(2,880,495)**	**(2,454,164)**

a. In 2013, following changes in industry practice governing client money, the accounting treatment in respect of client money held under the FCA's CASS Chapter 7 was revised. As at 31 December 2013, US$9.9 billion of cash at bank and in hand were no longer treated as the company's assets with a corresponding liability in other creditors.

26. ANALYSIS OF CHANGES IN NET DEBT

	31 December 2013	Cash Flows	Exchange Movements	31 December 2014
	US$'000	US$'000	US$'000	US$'000
Cash at bank and in hand	4,032,081	(254,369)	(191,570)	3,586,142
Overdrafts	(28,245)	19,608	-	(8,637)
Total cash	**4,003,836**	**(234,761)**	**(191,570)**	**3,577,505**
Long-term subordinated loans (see note 19)	(6,458,000)	-	-	(6,458,000)
Net borrowings	**(6,458,000)**	**-**	**-**	**(6,458,000)**
Net debt (see note 25)	**(2,454,164)**	**(234,761)**	**(191,570)**	**(2,880,495)**

27. FINANCIAL COMMITMENTS AND CONTINGENCIES

a. The table below presents the company's commitments.

	31 December 2014	31 December 2013
	US$'000	US$'000
Contingent and forward starting resale and securities borrowing agreements	34,571,820	39,828,253
Forward starting repurchase and secured lending agreements	14,760,347	20,820,153
Other	4,000,528	2,739,920
	53,332,695	**63,388,326**

The company enters into resale and securities borrowing agreements and repurchase and secured lending agreements that settle at a future date, generally within three business days. The company also enters into commitments to provide contingent financing to its clients and counterparties through resale agreements. The company's funding of these commitments depends on the satisfaction of all contractual conditions to the resale agreement and these commitments can expire unused.

Other commitments primarily relate to collateral commitments.

In addition, there are registered charges on the company's assets which have arisen in the ordinary course of business.

b. The company leases certain buildings on long-term leases. Under these leases, which are subject to renegotiation at various intervals specified in the leases, the company pays all insurance, maintenance and repairs of these properties. The rentals that the company is committed to pay in the next year are as follows:

	31 December 2014	31 December 2013
	US$'000	US$'000
Maturity of lease:		
Less than one year	107	909
Between one and two years	1,497	221
Between two and five years	6,957	1,274
Over five years	90,252	101,824
	98,813	**104,228**

27. FINANCIAL COMMITMENTS AND CONTINGENCIES (continued)

c. The company is involved in the below legal proceedings, however it is not practicable to estimate an impact, if any, of these proceedings.

i. The European Commission announced in April 2011 that it was initiating proceedings to investigate further numerous financial services companies, including GSI, in connection with the supply of data related to credit default swaps and in connection with profit sharing and fee arrangements for clearing of credit default swaps, including potential anticompetitive practices. On 1 July 2013, the European Commission issued to those financial services companies a Statement of Objections alleging that they colluded to limit competition in the trading of exchange-traded unfunded credit derivatives and exchange trading of credit default swaps more generally, and setting out its process for determining fines and other remedies. GSI's current understanding is that the proceedings related to profit sharing and fee arrangements for clearing of credit default swaps have been suspended indefinitely.

ii. Various alleged purchasers of, and counterparties involved in transactions relating to, mortgage pass-through certificates, CDOs and other mortgage-related products (including Aozora Bank, Ltd., Basis Yield Alpha Fund (Master), Deutsche Zentral-Genossenschaftbank and IKB Deutsche Industriebank AG) have filed complaints in the United States against the company and certain of its affiliates, generally alleging that the offering documents for the securities that they purchased contained untrue statements of material fact and material omissions and generally seeking rescission and / or damages. Certain of these complaints allege fraud and seek punitive damages.

iii. GSI is the defendant in an action filed on 21 January 2014 with the High Court of Justice in London by the Libyan Investment Authority, relating to nine derivative transactions between the plaintiff and GSI and seeking, among other things, rescission of the transactions and unspecified equitable compensation and damages exceeding US$1 billion. On 4 August 2014, GSI withdrew its 10 April 2014 motion for summary judgment, and on 4 December 2014, the Libyan Investment Authority filed an amended statement of claim.

iv. GSI is among the defendants in putative class actions, filed beginning 23 May 2014 in the U.S. District Court for the Southern District of New York, based on alleged violations of the federal antitrust laws in connection with the management of zinc storage facilities. The complaints seek declaratory, injunctive and other equitable relief as well as unspecified monetary damages, including treble damages.

v. GSI is among the defendants named in putative class actions relating to trading in platinum and palladium, filed beginning on 25 November 2014, in the U.S. District Court for the Southern District of New York. The complaints generally allege that the defendants violated federal antitrust laws and the Commodity Exchange Act in connection with an alleged conspiracy to manipulate a benchmark for physical platinum and palladium prices and seek declaratory and injunctive relief as well as treble damages in an unspecified amount.

28. FINANCIAL RISK MANAGEMENT AND CAPITAL MANAGEMENT

Certain disclosures required by U.K. GAAP in relation to the company's financial risk management and capital management have been presented alongside other risk management and regulatory information in Part 1 of this annual report.

29. FINANCIAL INSTRUMENTS

a. Financial instrument by category

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

	31 December 2014				
	Held for trading US$m	Designated at fair value US$m	Loans and receivables US$m	Amortised cost US$m	Total carrying value US$m
Financial assets:					
Financial instruments owned	667,823	-	-	-	667,823
Financial instruments owned pledged as collateral	24,404	-	-	-	24,404
Collateralised agreements	-	174,527	44,707	-	219,234
Debtors	-	1,780	75,362	-	77,142
Cash at bank and in hand	-	-	3,586	-	3,586
Total financial assets	**692,227**	**176,307**	**123,655**	**-**	**992,189**
Financial liabilities:					
Financial instruments sold, but not yet purchased	641,404	-	-	-	641,404
Collateralised financing	-	103,492	-	53,877	157,369
Other creditors	-	16,149	-	138,997	155,146
Creditors: amounts falling due after more than one year	-	5,899	-	10,801	16,700
Total financial liabilities	**641,404**	**125,540**	**-**	**203,675**	**970,619**

	31 December 2013				
	Held for trading US$m	Designated at fair value US$m	Loans and receivables US$m	Amortised cost US$m	Total carrying value US$m
Financial assets:					
Financial instruments owned	489,841	-	-	-	489,841
Financial instruments owned pledged as collateral	26,264	-	-	-	26,264
Collateralised agreements	-	173,448	52,406	-	225,854
Debtors	-	1,087	68,424	-	69,511
Cash at bank and in hand	-	-	4,032	-	4,032
Total financial assets	**516,105**	**174,535**	**124,862**	**-**	**815,502**
Financial liabilities:					
Financial instruments sold, but not yet purchased	457,164	-	-	-	457,164
Collateralised financing	-	134,795	-	55,416	190,211
Other creditors	-	18,946	-	114,170	133,116
Creditors: amounts falling due after more than one year	-	3,181	-	12,151	15,332
Total financial liabilities	**457,164**	**156,922**	**-**	**181,737**	**795,823**

29. FINANCIAL INSTRUMENTS (continued)

b. Fair value hierarchy

The table below presents, by level within the fair value hierarchy, financial assets and financial liabilities measured at fair value.

	31 December 2014			
	Level 1 US$m	Level 2 US$m	Level 3 US$m	Total US$m
Financial assets at fair value:				
Financial instruments owned, including financial instruments owned pledged as collateral	38,836	638,233	15,158	692,227
Collateralised agreements	-	174,527	-	174,527
Debtors	-	1,780	-	1,780
Total financial assets at fair value	**38,836**	**814,540**	**15,158**	**868,534**
Financial liabilities at fair value:				
Financial instruments sold, but not yet purchased	22,785	608,536	10,083	641,404
Collateralised financing	-	103,368	124	103,492
Other creditors	-	13,412	2,737	16,149
Creditors: amounts falling due after more than one year	-	5,056	843	5,899
Total financial liabilities at fair value	**22,785**	**730,372**	**13,787**	**766,944**

	31 December 2013			
	Level 1 US$m	Level 2 US$m	Level 3 US$m	Total US$m
Financial assets at fair value:				
Financial instruments owned, including financial instruments owned pledged as collateral	45,123	457,568	13,414	516,105
Collateralised agreements	-	173,448	-	173,448
Debtors	-	907	180	1,087
Total financial assets at fair value	**45,123**	**631,923**	**13,594**	**690,640**
Financial liabilities at fair value:				
Financial instruments sold, but not yet purchased	22,580	425,390	9,194	457,164
Collateralised financing	-	133,785	1,010	134,795
Other creditors	-	16,765	2,181	18,946
Creditors: amounts falling due after more than one year	-	2,694	487	3,181
Total financial liabilities at fair value	**22,580**	**578,634**	**12,872**	**614,086**

During 2014 and 2013, there were no significant transfers between level 1 and 2 financial assets and financial liabilities. The following tables present the changes in fair value for all the financial assets and financial liabilities categorised as level 3. Gains and losses arising on level 3 assets are recognised within net revenue in the profit and loss account.

If a financial asset or financial liability was transferred to level 3 during a reporting year, its entire gain or loss for the year is included in level 3. Transfers between levels are recognised at the beginning of the reporting year in which they occur. Accordingly, the tables do not include gains or losses that were reported in level 3 in prior year for financial assets and financial liabilities that were transferred out of level 3 prior to the end of the year.

29. FINANCIAL INSTRUMENTS (continued)

b. Fair value hierarchy (continued)

Level 3 financial instruments are frequently economically hedged with level 1, level 2 and level 3 financial instruments. Accordingly, gains or losses that are reported in level 3 can be partially offset by gains or losses attributable to level 1, level 2 or level 3 instruments. As a result, gains or losses included in the level 3 rollforward below do not necessarily represent the overall impact on the company's results of operations, liquidity or capital resources.

Reconciliation of level 3 financial assets at fair value:	Financial instruments owned, including financial instruments owned pledged as collateral US$m	Debtors US$m	Total financial assets at fair value US$m
At 1 January 2014	13,414	180	13,594
Profit for the year	4,423	-	4,423
Purchases	2,028	-	2,028
Sales	(771)	-	(771)
Settlements	(5,096)	-	(5,096)
Transfers into level 3	2,759	-	2,759
Transfers out of level 3	(1,599)	(180)	(1,779)
At 31 December 2014	**15,158**	**-**	**15,158**

Reconciliation of level 3 financial liabilities at fair value:	Financial instruments sold, but not yet purchased US$m	Collateralised financing US$m	Other creditors and creditors: amounts falling due after more than one year US$m	Total financial liabilities at fair value US$m
At 1 January 2014	9,194	1,010	2,668	12,872
Profit for the year	2,336	-	(132)	2,204
Purchases	(5)	-	2	(3)
Sales	982	-	2,954	3,936
Settlements	(3,180)	(886)	(1,773)	(5,839)
Transfers into level 3	2,293	-	447	2,740
Transfers out of level 3	(1,537)	-	(586)	(2,123)
At 31 December 2014	**10,083**	**124**	**3,580**	**13,787**

During 2014, level 3 transfers into financial assets of US$2.8 billion and financial liabilities of US$2.7 billion primarily reflect transfers of certain credit derivatives from level 2, principally due to reduced transparency of the correlation inputs used to value these derivatives as a result of less observable trading activity, and transfers of certain other credit derivatives from level 2, principally due to unobservable credit spread inputs becoming significant to the valuation of these instruments.

During 2014, level 3 transfers out of financial assets of US$1.8 billion and financial liabilities of US$2.1 billion primarily reflect transfers of certain credit derivatives to level 2, principally due to unobservable correlation inputs no longer being significant to the valuation of these derivatives, and the transfers of certain credit derivatives to level 2, principally due to unobservable credit spread inputs no longer being significant to the net risk of certain portfolios.

29. FINANCIAL INSTRUMENTS (continued)

b. Fair value hierarchy (continued)

Reconciliation of level 3 financial assets at fair value:	**Financial instruments owned, including financial instruments owned pledged as collateral US$m**	**Debtors US$m**	**Total financial assets at fair value US$m**
At 1 January 2013	16,075	166	16,241
Profit for the year	996	14	1,010
Purchases	1,601	-	1,601
Sales	(1,307)	-	(1,307)
Settlements	(4,482)	-	(4,482)
Transfers into level 3	2,463	-	2,463
Transfers out of level 3	(1,932)	-	(1,932)
At 31 December 2013	**13,414**	**180**	**13,594**

Reconciliation of level 3 financial liabilities at fair value:	**Financial instruments sold, but not yet purchased US$m**	**Collateralised financing US$m**	**Other creditors and creditors: amounts falling due after more than one year US$m**	**Total financial liabilities at fair value US$m**
At 1 January 2013	9,915	1,927	2,390	14,232
Profit for the year	1,272	-	99	1,371
Purchases	(8)	-	(3)	(11)
Sales	581	-	1,694	2,275
Settlements	(3,136)	(917)	(1,540)	(5,593)
Transfers into level 3	1,937	-	315	2,252
Transfers out of level 3	(1,367)	-	(287)	(1,654)
At 31 December 2013	**9,194**	**1,010**	**2,668**	**12,872**

During 2013, level 3 transfers into financial assets of US$2.5 billion and financial liabilities of US$2.3 billion primarily reflect transfers of certain credit derivatives from level 2, principally due to reduced transparency of upfront credit points and correlation inputs used to value these derivatives.

During 2013, level 3 transfers out of financial assets of US$1.9 billion and financial liabilities of US$1.7 billion primarily reflect transfers of certain credit derivatives to level 2, principally due to unobservable credit spread and correlation inputs no longer being significant to the valuation of these derivatives and unobservable inputs not being significant to the net risk of certain portfolios.

29. FINANCIAL INSTRUMENTS (continued)

c. Fair value financial instruments valued using techniques that incorporate unobservable inputs

The fair value of financial instruments may be determined in whole or part using a valuation technique based on assumptions that are not supported by prices from observable current market transactions in the same instrument or based on available observable market data and changing these assumptions will change the resultant estimate of fair value. The potential impact as at 31 December 2014 of using reasonable possible alternative assumptions for the valuations including significant unobservable inputs has been quantified as approximately US$179 million (2013: US$113 million) for favourable changes and US$146 million (2013: US$127 million) for unfavourable changes. In determining reasonably possible alternative unfavourable assumptions a detailed business and position level review has been performed to identify and quantify instances where potential uncertainty exists. This has taken into account the positions' current value as compared to the range of available market information.

The amounts not recognised in the profit and loss account relating to the difference between the fair value of financial instruments held for trading at initial recognition (the transaction price) and the amounts determined at initial recognition using the valuation techniques ('Day 1 P&L') are as follows:

	2014 US$m	2013 US$m
At 1 January	80	104
New transactions	118	44
Amounts recognised in the profit and loss account during the year	(62)	(68)
At 31 December	**136**	80

d. Fair value of financial instruments not measured at fair value

The company has US$123.7 billion (2013: US$124.9 billion) of current financial assets and US$192.9 billion (2013: US$169.6 billion) of current financial liabilities that are not measured at fair value. Given the short-term nature of these instruments, their carrying amounts in the balance sheet are a reasonable approximation of fair value.

The company has US$10.8 billion (2013: US$12.2 billion) of financial liabilities that are due after more than one year that are not measured at fair value which predominantly relate to long-term intercompany borrowings. The interest rates of these borrowings are variable in nature and approximate prevailing market interest rates for instruments with similar terms and characteristics. As such, their carrying amounts in the balance sheet are a reasonable approximation of fair value.

29. FINANCIAL INSTRUMENTS (continued)

e. Maturity of financial liabilities

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

	31 December 2014						
	Trading / On Demand US$m	Less than one month US$m	More than one month but less than three months US$m	More than three months but less than one year US$m	More than one year but less than five years US$m	Greater than five years US$m	Total US$m
Financial liabilities:							
Financial instruments sold, but not yet purchased	641,404	-	-	-	-	-	641,404
Collateralised financing	74,056	63,446	7,071	10,282	2,418	96	157,369
Other creditors	91,919	13,196	439	50,068	-	-	155,622
Creditors: amounts falling due after more than one year	-	2	4	26	9,110	8,675	17,817
Total – on-balance-sheet	**807,379**	**76,644**	**7,514**	**60,376**	**11,528**	**8,771**	**972,212**
Contingent and forward starting resale and securities borrowing agreements	-	34,572	-	-	-	-	34,572
Operating leases	-	8	16	74	385	80	563
Other	4,001	-	-	-	-	-	4,001
Total – commitments	**4,001**	**34,580**	**16**	**74**	**385**	**80**	**39,136**
Total	**811,380**	**111,224**	**7,530**	**60,450**	**11,913**	**8,851**	**1,011,348**

29. FINANCIAL INSTRUMENTS (continued)

e. Maturity of financial liabilities (continued)

	31 December 2013						
	Trading / On Demand US$m	Less than one month US$m	More than one month but less than three months US$m	More than three months but less than one year US$m	More than one year but less than five years US$m	Greater than five years US$m	Total US$m
Financial liabilities:							
Financial instruments sold, but not yet purchased	457,164	-	-	-	-	-	457,164
Collateralised financing	84,331	71,878	13,645	17,708	1,000	1,649	190,211
Other creditors	75,934	14,126	2,331	41,173	-	-	133,564
Creditors: amounts falling due after more than one year	-	2	4	28	7,770	8,719	16,523
Total – on-balance-sheet	**617,429**	**86,006**	**15,980**	**58,909**	**8,770**	**10,368**	**797,462**
Contingent and forward starting resale and securities borrowing agreements	-	39,828	-	-	-	-	39,828
Operating leases	-	9	17	78	409	184	697
Other	2,740	-	-	-	-	-	2,740
Total – commitments	**2,740**	**39,837**	**17**	**78**	**409**	**184**	**43,265**
Total	**620,169**	**125,843**	**15,997**	**58,987**	**9,179**	**10,552**	**840,727**

f. Collateral

The company receives financial instruments (e.g., government and agency obligations, corporate debt securities, equities and convertible debentures) as collateral, primarily in connection with resale agreements, securities borrowed, derivative transactions and customer margin loans. The company obtains cash and securities as collateral on an upfront or contingent basis for derivative instruments and collateralised agreements to reduce its credit exposure to individual counterparties.

In many cases, the company is permitted to deliver or repledge financial instruments received as collateral when entering into repurchase agreements and securities lending agreements, primarily in connection with secured client financing activity. The company is also permitted to deliver or repledge these financial instruments in connection with other secured financings, collateralising derivative transactions and meeting company or customer settlement requirements.

The table below presents financial instruments received as collateral that were available to be delivered, or repledged and were delivered or repledged by the company.

	31 December 2014 US$m	31 December 2013 US$m
Collateral available to be delivered or repledged	369,545	342,641
Collateral that was delivered or repledged	294,994	279,698

29. FINANCIAL INSTRUMENTS (continued)

f. Collateral (continued)

The company also pledges certain financial instruments owned in connection with repurchase agreements, securities lending agreements and other secured financings to counterparties who may or may not have the right to deliver or repledge. Financial instruments owned and pledged to counterparties that have the right to deliver or repledge are included within 'Financial instruments owned pledged as collateral' in the balance sheet, whereas financial instruments owned and pledged to counterparties that did not have the right to sell or pledge are included in 'Financial instruments owned' in the balance sheet. The table below presents information about financial instruments pledged to counterparties by the company.

	31 December 2014 Carrying amount US$m	31 December 2013 Carrying amount US$m
That had the right to deliver or repledge	24,404	26,264
That did not have the right to deliver or repledge	17,656	22,360

The company has received cash collateral in respect of financial instruments owned of US$57.5 billion (2013: US$45.8 billion) and posted cash collateral in respect of financial instruments sold, but not yet purchased of US$35.5 billion (2013: US$28.6 billion).

In addition to repurchase agreements and securities lending transactions, the company funds certain assets through the use of other secured financings and pledges financial instruments as collateral in these transactions. These other secured financings consist of liabilities related to special purpose entities, transfers of financial assets that are accounted for as financings rather than sales and other structured financing arrangements. Other secured financings include arrangements that are non-recourse.

g. Transferred assets

Assets continued to be recognised in full

During the year, the company transferred certain financial assets where the transfers failed to meet the derecognition criteria, as contained in FRS26 (IAS39) 'Financial Instruments: Recognition and Measurement', and as a result of which the company continues to recognise these assets in full on the balance sheet.

The company transfers assets owned to counterparties in the ordinary course of business to collateralise repurchase agreements and other securities lending transactions. In these transactions the transferred assets continue to be recognised by the company for accounting purposes because the transactions require the financial instruments to be repurchased at maturity of the agreement and the company remains exposed to the price, credit and interest rate risk of these instruments. When the company receives cash proceeds from the transfer of the asset, a financial liability is recognised in respect of the consideration received and recorded within 'collateralised financing'. When the company receives non-cash collateral (in the form of securities) no liability is initially recognised. If collateral received is subsequently sold, the obligation to return the collateral is recognised as a liability within 'Financial instruments sold, but not yet purchased'.

In addition to repurchase agreements and securities lending agreements, the company obtains funding through the use of other arrangements that fail to meet the derecognition criteria. For example, sales of securities with related derivatives, such as total return swaps, through which the company retains substantially all of the risk and reward of the transferred assets. A financial liability is recognised in such cases for the proceeds received.

Other financial assets transferred that continue to be recognised on balance sheet for accounting purposes relate to pledges of securities as collateral, primarily for derivative transactions. The obligations under such derivatives are recorded in 'Financial instruments sold, but not yet purchased'.

29. FINANCIAL INSTRUMENTS (continued)

g. Transferred assets (continued)

The following table presents financial assets which have been transferred but which remain on balance sheet for accounting purposes. The carrying amount of the associated financial liabilities generally approximate the carrying amount of the assets transferred.

	31 December 2014 Carrying amount US$m	31 December 2013 Carrying amount US$m
Commercial paper, certificates of deposit, time deposits and other money market instruments	1,047	1,940
Government and agency obligations	11,095	10,518
Mortgage and other asset-backed loans and securities	-	95
Corporate and other debt obligations	6,248	7,326
Equities and convertible debentures	23,670	28,745
	42,060	**48,624**

Derecognised assets with ongoing exposure

The company has continuing involvement in the form of derivative transactions and guarantees with certain non-consolidated structured entities to which the company had transferred financial assets. These derivatives may be credit-linked to the asset transferred and result in the company retaining specific risks in the transferred asset or require the company to make payments to the structured entity to compensate losses on the asset if certain contingent events occur.

In addition, the company transfers financial assets to securitisation vehicles. The company generally receives cash in exchange for the transferred assets but may have continuing involvement with the transferred assets, including ownership of beneficial interests in the securitisation. The company may also purchase senior or subordinated securities issued by securitisation vehicles in connection with secondary market-making activities.

The following disclosures provide further information about the company's exposure through this continuing involvement. In all cases these retained interests are carried at fair value.

	31 December 2014		31 December 2013	
	Carrying amount US$m	Maximum exposure to loss US$m	Carrying amount US$m	Maximum exposure to loss US$m
Financial instruments owned:				
Derivative instruments	120	1,308	62	1,395
Cash instruments	64	64	142	142
Financial instruments sold, but not yet purchased:				
Derivative instruments	(2)	(92)	(31)	(235)
Other liabilities	-	-	-	-

Where the company's continuing involvement in transferred assets is through derivatives or guarantees, the maximum exposure to loss is the notional amounts of the derivative or guarantee. For retained or purchased interests in securitised assets, the company's risk of loss is limited to the fair value of these interests.

29. FINANCIAL INSTRUMENTS (continued)

g. Transferred assets (continued)

For transactions with continuing involvement, the following table shows information about the gains or losses.

	31 December 2014		31 December 2013	
	Income / (expense) in the year US$m	Cumulative income / (expense) US$m	Income / (expense) in the year US$m	Cumulative income / (expense) US$m
Financial instruments owned:				
Derivative instruments	66	144	2	78
Cash instruments	27	119	63	92
Financial instruments sold, but not yet purchased:				
Derivative instruments	2	(31)	(5)	(33)
Other liabilities	-	(1)	-	(1)

The company accounts for assets pending transfer at fair value and therefore does not typically recognise significant gains or losses upon the transfer of assets. The company does not have continuing involvement that could require the company to repurchase derecognised financial assets.

h. Hedge accounting

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

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

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

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

	31 December 2014 US$'000	31 December 2013 US$'000
Interest rate hedges	84,870	(20,367)
Hedged borrowings	(79,931)	18,119
Hedge ineffectiveness	**4,939**	**(2,248)**

The fair value of asset and liability derivative instruments designated as hedges were US$188 million and US$10 million, respectively, as at 31 December 2014 (2013: assets of US$113 million and liabilities of US$40 million).

30. OTHER ITEMS

Basel III Pillar 3 disclosures

The company is included in the consolidated Pillar 3 disclosures of GSGUK, which are required by the EU Capital Requirements Regulation. GSGUK's 2014 Pillar 3 disclosures will be made available, in conjunction with the publication of its financial statements, at www.goldmansachs.com/disclosures/.

Country-by-country reporting

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

31. ULTIMATE AND IMMEDIATE PARENT UNDERTAKINGS

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

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