



**Citizens**  
Financial Group, Inc.

**Consolidated Financial Statements**

**2010**



## 2010 Consolidated Financial Statements

### Table of Contents

	<i><u>Page</u></i>
Independent Auditors' Report .....	1
Consolidated Balance Sheets .....	2
Consolidated Statements of Operations .....	3
Consolidated Statements of Changes in Stockholder's Equity .....	4
Consolidated Statements of Cash Flows .....	5
Notes To Consolidated Financial Statements	
Note 1 Significant Accounting Policies .....	6
Note 2 Cash and Due From Banks .....	13
Note 3 Securities .....	14
Note 4 Loans and Leases.....	18
Note 5 Allowance for Credit Losses and Concentrations of Credit Risk....	19
Note 6 Nonperforming Assets .....	23
Note 7 Premises and Equipment .....	25
Note 8 Lease Commitments .....	25
Note 9 Goodwill and Intangible Assets .....	26
Note 10 Mortgage Banking .....	27
Note 11 Deposits .....	29
Note 12 Borrowed Funds .....	30
Note 13 Preferred Stock .....	31
Note 14 Employee Benefits .....	31
Note 15 Income Taxes .....	38
Note 16 Derivatives .....	41
Note 17 Commitments, Guarantees and Contingencies .....	45
Note 18 Divestitures and Discontinued Operations.....	47
Note 19 Related Party Transactions .....	48
Note 20 Fair Value Measurements .....	49
Note 21 Regulatory Matters .....	55
Note 22 Supplemental Information .....	56
Note 23 Exit Costs and Restructuring Reserves.....	57
Note 24 Subsequent Events.....	57



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## **INDEPENDENT AUDITORS' REPORT**

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

We have audited the accompanying consolidated balance sheets of Citizens Financial Group, Inc. and subsidiaries (the "Company") as of December 31, 2010 and 2009, and the related consolidated statements of operations, changes in stockholder's equity, and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, such consolidated financial statements present fairly, in all material respects, the financial position of the Company as of December 31, 2010 and 2009, and the results of its operations and its cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America.

A handwritten signature in black ink that reads "Deloitte &amp; Touche LLP". The signature is written in a cursive, slightly slanted style.

February 22, 2011

**CITIZENS FINANCIAL GROUP, INC.**  
**CONSOLIDATED BALANCE SHEETS**  
**As of December 31, 2010 and 2009**

<i>(in millions, except share data)</i>	<b>2010</b>	<b>2009</b>
<b>ASSETS:</b>		
Cash and due from banks	\$4,918	\$7,084
Interest-bearing deposits in banks	163	141
Securities available-for-sale, at fair value	20,549	26,835
Other investment securities	1,253	1,326
Mortgage loans held-for-sale, at fair value	716	456
Credit card loans held-for-sale, at lower of cost or fair value	-	518
Loans and leases	87,022	95,080
Less: Allowance for loan and lease losses	2,005	2,209
Net loans and leases	85,017	92,871
Goodwill	11,311	11,311
Other intangibles	51	132
Bank-owned life insurance	1,214	1,170
Derivative assets	1,082	1,033
Premises and equipment	1,041	1,006
Accrued interest receivable	410	510
Deferred taxes, net	327	550
Mortgage servicing rights	193	179
Other assets	1,444	1,530
Assets of discontinued operations	-	1,029
<b>TOTAL ASSETS</b>	<b>\$129,689</b>	<b>\$147,681</b>
<b>LIABILITIES AND STOCKHOLDER'S EQUITY:</b>		
<b>LIABILITIES:</b>		
Deposits	\$92,155	\$98,053
Federal funds purchased and securities sold under agreements to repurchase	5,112	5,222
Borrowed funds	7,784	18,508
Due to broker	693	-
Derivative liabilities	117	1,922
Other liabilities	1,134	1,091
Liabilities of discontinued operations	-	609
<b>TOTAL LIABILITIES</b>	<b>106,995</b>	<b>125,405</b>
<b>STOCKHOLDER'S EQUITY:</b>		
Preferred stock:		
\$1.00 par value, 30,000 shares authorized, no shares outstanding in 2010 and 2009	-	-
Common stock:		
\$.01 par value, 5,000 shares authorized, 3,382 shares issued and outstanding in 2010 and 2009	-	-
Additional paid-in capital	18,538	18,538
Retained earnings	4,847	4,836
Accumulated other comprehensive loss	(691)	(1,098)
<b>TOTAL STOCKHOLDER'S EQUITY</b>	<b>22,694</b>	<b>22,276</b>
<b>TOTAL LIABILITIES AND STOCKHOLDER'S EQUITY</b>	<b>\$129,689</b>	<b>\$147,681</b>

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

**CITIZENS FINANCIAL GROUP, INC.**  
**CONSOLIDATED STATEMENTS OF OPERATIONS**  
**For Years Ended December 31, 2010 and 2009**

<i>(in millions)</i>	2010	2009
<b>INTEREST INCOME:</b>		
Interest and fees on loans and leases:		
Consumer	\$2,010	\$2,436
Commercial	830	899
Residential mortgage	530	683
Commercial real estate	287	323
Credit card	183	227
Loans held for sale	18	21
Investment securities	881	1,212
Interest-bearing deposits in banks	14	13
<b>Total interest income</b>	<b>4,753</b>	<b>5,814</b>
<b>INTEREST EXPENSE:</b>		
Deposits	632	1,301
Federal funds purchased and securities sold under agreements to repurchase	475	521
Borrowed funds	301	573
<b>Total interest expense</b>	<b>1,408</b>	<b>2,395</b>
Net interest income	3,345	3,419
Provision for credit losses	1,644	2,783
<b>Net interest income after provision for credit losses</b>	<b>1,701</b>	<b>636</b>
<b>NONINTEREST INCOME:</b>		
Service charges on deposits	628	715
Net gains on sales of securities available for sale	419	29
ATM and debit card	284	241
Mortgage banking	145	154
Other service fee income	144	118
International fees	114	120
Credit card fees	93	107
Investment services revenue	91	81
Bank-owned life insurance	49	49
Other leasing income	36	30
Trust income	25	26
Customer derivatives	18	(2)
Other-than-temporary impairment:		
Total other-than-temporary impairment losses	(164)	(134)
Portions of loss recognized in other comprehensive income (before taxes)	147	125
<b>Net impairment losses recognized in earnings</b>	<b>(17)</b>	<b>(9)</b>
Other net losses	(331)	(8)
Other income	35	15
<b>Total noninterest income</b>	<b>1,733</b>	<b>1,666</b>
<b>NONINTEREST EXPENSE:</b>		
Salaries and employee benefits	1,637	1,542
Equipment expense	357	358
Outside services	312	296
Occupancy	335	321
Amortization of intangibles	81	141
Promotional expense	124	122
Other operating expense	637	715
<b>Total noninterest expense</b>	<b>3,483</b>	<b>3,495</b>
Loss from continuing operations before income tax benefit	(49)	(1,193)
Income tax benefit from continuing operations	(61)	(420)
<b>Income (loss) from continuing operations</b>	<b>12</b>	<b>(773)</b>
Income from discontinued operations	26	52
Loss on sale of discontinued operations	(11)	-
Income tax expense from discontinued operations	16	19
<b>(Loss) income from discontinued operations</b>	<b>(1)</b>	<b>33</b>
<b>NET INCOME (LOSS)</b>	<b>\$11</b>	<b>(\$740)</b>

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

**CITIZENS FINANCIAL GROUP, INC.**  
**CONSOLIDATED STATEMENTS OF CHANGES IN STOCKHOLDER'S EQUITY**  
**As of and for Years Ended December 31, 2010 and 2009**

<i>(in millions)</i>	Preferred Stock	Common Stock	Additional Paid-in Capital	Retained Earnings	Accumulated Other Comprehensive Income (Loss)	Total
<b>Balance at December 31, 2008</b>	\$1,585	\$0	\$15,223	\$5,576	(\$2,432)	\$19,952
Cancellation of preferred stock	(1,585)	-	1,585	-	-	-
Conversion of subordinated debt	-	-	1,730	-	-	1,730
Comprehensive income (loss):						
Net loss from continuing operations	-	-	-	(773)	-	(773)
Net income from discontinued operations	-	-	-	33	-	33
Other comprehensive income	-	-	-	-	1,334	1,334
Total comprehensive income						594
<b>Balance at December 31, 2009</b>	-	-	18,538	4,836	(1,098)	22,276
Comprehensive income (loss):						
Net income from continuing operations	-	-	-	12	-	12
Net income from discontinued operations	-	-	-	10	-	10
Loss on sale of discontinued operations	-	-	-	(11)	-	(11)
Other comprehensive income	-	-	-	-	407	407
Total comprehensive income						418
<b>Balance at December 31, 2010</b>	\$0	\$0	\$18,538	\$4,847	(\$691)	\$22,694

<i>(in millions)</i>	Net Unrealized Gains (Losses) on Derivatives	Net Unrealized Gains (Losses) on Securities	Pension Liability	Accumulated Other Comprehensive Income (Loss)
<b>Balance at December 31, 2008</b>	(\$1,728)	(\$435)	(\$269)	(\$2,432)
Net unrealized derivative instrument gains arising during the period, net of taxes	45	-	-	45
Reclassification adjustment for net derivative losses included in net loss, net of taxes	712	-	-	712
Net unrealized securities gains arising during the period, net of taxes	-	572	-	572
Reclassification of net securities gains to net loss, net of taxes	-	(11)	-	(11)
Defined benefit pension plans:				
Actuarial gain, net of taxes	-	-	13	13
Amortization of prior service credit, net of taxes	-	-	(3)	(3)
Amortization of actuarial loss, net of taxes	-	-	35	35
Transfer of merged plans	-	-	(29)	(29)
<b>Balance at December 31, 2009</b>	(971)	126	(253)	(1,098)
Net unrealized derivative instrument losses arising during the period, net of taxes	(425)	-	-	(425)
Reclassification adjustment for net derivative losses included in net income, net of taxes	754	-	-	754
Net unrealized securities gains arising during the period, net of taxes	-	291	-	291
Reclassification of net securities gains to net income, net of taxes	-	(254)	-	(254)
Defined benefit pension plans:				
Actuarial loss, net of taxes	-	-	(53)	(53)
Amortization of prior service credit, net of taxes	-	-	(2)	(2)
Amortization of actuarial loss, net of taxes	-	-	17	17
Curtailement, net of taxes	-	-	79	79
<b>Balance at December 31, 2010</b>	(\$642)	\$163	(\$212)	(\$691)

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

**CITIZENS FINANCIAL GROUP, INC.**  
**CONSOLIDATED STATEMENTS OF CASH FLOWS**  
**For Years Ended December 31, 2010 and 2009**

<i>(in millions)</i>	2010	2009
<b>OPERATING ACTIVITIES</b>		
Net income (loss)	\$11	(\$740)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Provision for credit losses	1,644	2,783
Originations of loans held for sale	(5,171)	(5,245)
Proceeds from sales of loans held for sale	4,911	4,927
Amortization of terminated cash flow hedges	565	605
Depreciation, amortization and accretion	405	525
Valuation of mortgage servicing rights	15	(23)
Net loss on investment securities	16	25
Deferred income taxes	24	(40)
Loss on disposal/impairment of premises and equipment	27	47
Loss (gain) on sales of:		
Securities available-for-sale	(419)	(29)
Subsidiary	11	-
Branch network	-	(8)
Decrease (increase) in:		
Accrued interest receivable	100	161
Other assets	33	(127)
Decrease in other liabilities	(271)	(841)
Net cash provided by operating activities of continuing operations	1,901	2,020
Net cash (used in) provided by operating activities of discontinued operations	(155)	52
<b>INVESTING ACTIVITIES</b>		
Investment securities:		
Purchases of securities available-for-sale	(6,842)	(7,166)
Proceeds from maturities and paydowns of securities available-for-sale	6,639	6,368
Proceeds from sales of securities available-for-sale	7,572	2,612
Purchases of other investment securities	(2)	(45)
Proceeds from sales of other investment securities	78	82
Net (increase) decrease in interest-bearing deposits in banks	(22)	56
Net increase in cash collateral	(1,485)	-
Net decrease in loans and leases	6,661	11,723
Net increase in bank-owned life insurance	(44)	(36)
Net cash payments for divestiture activities	-	(375)
Premises and equipment:		
Purchases	(295)	(216)
Proceeds from sales	3	5
Net cash provided by investing activities of continuing operations	12,263	13,008
Net cash provided by (used in) investing activities of discontinued operations	557	(18)
<b>FINANCING ACTIVITIES</b>		
Net (decrease) increase in deposits	(5,898)	3,871
Net decrease in federal funds purchased and securities sold under agreements to repurchase	(110)	(179)
Proceeds from borrowed funds	80,498	233,622
Repayments of borrowed funds	(91,222)	(248,310)
Net cash used in financing activities of continuing operations	(16,732)	(10,996)
(Decrease) increase in cash and cash equivalents	(2,166)	4,066
Cash and cash equivalents at beginning of period	7,084	3,018
Cash and cash equivalents at end of period	\$4,918	\$7,084

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**1. SIGNIFICANT ACCOUNTING POLICIES**

The accounting and reporting policies of Citizens Financial Group, Inc. and subsidiaries (the “Company”) conform to accounting principles generally accepted in the United States of America (“GAAP”). The Company is ultimately a wholly-owned subsidiary of The Royal Bank of Scotland Group plc. The Royal Bank of Scotland Group plc and its subsidiary entities are collectively referred to herein as “RBSG”. On December 1, 2008, the UK Government became the ultimate controlling party of RBSG. The UK Government’s shareholding is managed by UK Financial Investments Limited, a company wholly owned by the UK Government.

The Company's principal business activity is banking, conducted through its subsidiaries RBS Citizens, N.A.; Citizens Bank of Pennsylvania; RBS Asset Finance, Inc. and CCO Investment Services Corp. RBS WorldPay, Inc., a wholly-owned subsidiary of Citizens Financial Group, Inc., was sold on November 30, 2010. See Note 18.

The following is a summary of the significant accounting policies of the Company.

***Basis of Presentation***

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

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

***Cash and Cash Equivalents***

For the purposes of reporting cash flows, cash and cash equivalents includes cash and due from banks, federal funds sold and securities purchased under agreements to resell with original maturities of three months or less.

***Interest-Bearing Deposits***

Interest-bearing deposits are carried at cost and include deposits that mature within one year and money market mutual fund investments.

***Securities***

Investments in debt and equity securities are carried in three portfolios: available-for-sale, trading account assets and other investment securities. Management determines the appropriate classification at the time of purchase. Securities in the available-for-sale portfolio will be held for indefinite periods of time and may be sold in response to changes in interest rates, changes in prepayment risk, or other factors in managing the Company’s asset/liability strategy. Gains and losses on the sales of securities are recognized in earnings and are computed using the specific identification method. Security impairments (i.e. declines in the fair value of securities below cost) that are considered by management to be other-than-temporary are recognized in earnings as realized losses. However, the determination of the impairment amount is dependent on the Company’s intent to sell (or not sell) the security. If the Company intends to sell the impaired security, the impairment loss recognized in current period earnings equals the difference between the instrument’s fair value and its amortized cost. If the Company does not intend to sell the impaired security, and it is not likely



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

that the Company will be required to sell the impaired security, the credit-related impairment loss is recognized in current period earnings and equals the difference between the amortized cost of the security and the present value of the expected cash flows that have currently been projected.

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

Debt and equity securities that are bought and held principally for the purpose of selling them in the near term are classified as trading account assets and are carried at fair value. Realized and unrealized gains and losses on such assets are reported in noninterest income on the consolidated statements of operations. Trading account assets are reported in other assets on the consolidated balance sheets.

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

***Loans and Leases***

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

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

Credit card loans held for sale are recorded at the lower of cost or fair value.

Loans and leases are disclosed in portfolio segments and classes. The Company’s loan segments are commercial and retail. The classes of loans and leases are commercial; commercial real estate; leases; home equity products serviced by others (i.e. purchased home equity loans and lines of credit); residential (i.e. residential mortgages and home equity loans and lines of credit originated by the Company); other secured retail (i.e. automobile loans, student loans, other installment loans); and unsecured retail (i.e. credit card).

***Allowance for Credit Losses***

Management’s estimate of probable losses in the Company’s loan portfolios is recorded in the allowance for loan and lease losses and the reserve for unfunded lending commitments.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The Company evaluates the adequacy of the allowance for loan and lease losses by performing reviews of certain individual loans and leases, analyzing changes in the composition, size and delinquency of the portfolio, reviewing previous loss experience, and considering current and anticipated economic factors.

The allowance is maintained at a level which management considers to be adequate based on the results of this evaluation, and is established through charges to earnings in the form of a provision for credit losses. Amounts determined to be uncollectible are deducted from the allowance and subsequent recoveries, if any, are added to the allowance. While management uses available information to estimate loan losses, future additions to the allowance may be necessary based on changes in economic conditions. In addition, various regulatory agencies, as an integral part of their examination process, periodically review the Company's allowance for credit losses. Such agencies may require the Company to recognize changes to the allowance based on their judgment of information available to them at the time of their examination.

The allowance for loan and lease losses includes allocated and unallocated reserves. The allocated reserve is attributable to certain individual impaired loans and to pools of loans. The reserve for pools of loans is calculated using models sensitive to credit factors such as loan payment status and historical loss rates adjusted to reflect current conditions. The unallocated reserve provides a supplemental contingency for the allocated reserve and protects against latent or embedded losses in the overall loan portfolio and model imprecision. It reflects factors that apply to the portfolio as a whole and that are difficult to attribute to individually impaired loans or to groups of loans. These factors include changing underwriting criteria, purchased loan portfolios, changes in the types and mix of loans originated, industry concentrations and evaluations, allowance levels relative to selected overall credit criteria and other economic indicators used to estimate probable incurred losses.

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

The allowance for loan and lease losses and the reserve for unfunded lending commitments are reported on the consolidated balance sheets in the allowance for loan and lease losses and in other liabilities, respectively. Provision for credit losses related to the loans and leases portfolio and the unfunded lending commitments are reported in the consolidated statements of operations as provision for credit losses.

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

***Nonperforming Loans and Leases***

Commercial loans, commercial real estate loans, and leases are generally placed on nonaccrual status when contractually past due 90 days or more, or earlier if management believes that the probability of collection is insufficient to warrant further accrual. Some of these loans and leases may remain on accrual status when contractually past due 90 days or more if management considers the loan collectible. A loan may be returned to accrual status if (1) principal and interest payments have been brought current, and the Company expects repayment of the remaining contractual principal and interest, or (2) the loan or lease has otherwise become well-secured and in the process of collection, or (3) the borrower has been making regularly

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

scheduled payments in full for the prior six months and it's reasonably assured that the loan or lease will be brought fully current within a reasonable period.

Residential mortgages are generally placed on nonaccrual status when 90 days past due. A residential mortgage may also be placed on nonaccrual status if there is negative equity and a partial charge-off is recorded, or if foreclosure action could result in negative equity (these are defined as watch loans). Residential mortgages are returned to accrual status when principal and interest payments are brought current and when future payments are reasonably assured, following a sustained period of repayment performance by the borrower in accordance with the contractual terms.

Home equity loans and lines of credit, home equity products serviced by others, automobile loans, and other installment loans are generally placed on nonaccrual status when past due 90 days or more. Loans less than 90 days past due may be placed on nonaccrual status upon the death of the borrower, surrender or repossession of collateral, or bankruptcy. Non-guaranteed student loans are placed on nonaccrual status when they become 90 days past due or in the event of fraud, bankruptcy, or the borrower's death. A loan may be returned to accrual status if the loan becomes less than 15 days past due. Guaranteed student loans are not placed on nonaccrual status. Credit card balances are placed on nonaccrual status when past due 90 days or more. They are restored to accruing status if they subsequently become less than 90 days past due.

Cash receipts on nonaccruing loans and leases are generally applied to reduce the unpaid principal balance.

***Impaired Loans***

A loan is considered to be impaired when it is probable that the Company will be unable to collect all of the contractual interest and principal payments as scheduled in the loan agreement. Impaired loans include nonaccruing larger balance (greater than \$3 million carrying value in 2010 and greater than \$1 million carrying value in 2009), non-homogenous commercial and commercial real estate loans, and restructured loans which are deemed troubled debt restructurings ("TDRs"). A loan is identified as a TDR when the Company grants the borrower a concession the Company would not otherwise make in response to the borrower's financial difficulties. Concessions granted in TDRs for all classes of loans may include lowering the interest rate, forgiving a portion of principal, extending the loan term, lowering scheduled payments for a specified period of time, or capitalizing arrearages. TDRs for commercial loans and leases may also involve creating a multiple note structure, accepting non-cash assets, accepting an equity interest, or receiving a performance-based fee. The financial effects of TDRs for all loan classes may include lower income (either due to a lower interest rate or a delay in the timing of cash flows), larger loan loss provisions, and accelerated charge-offs if the loan is collateral-dependent.

Impairment evaluations are performed at the individual loan level, and consider expected future cash flows from the loan, including, if appropriate, the realizable value of collateral. Impaired loans which are not TDRs are nonaccruing, and loans involved in TDRs may be accruing or nonaccruing. Cash receipts on nonaccruing impaired loans, including nonaccruing loans involved in TDRs, are generally applied to reduce the unpaid principal balance. Loans are restored to accrual status when principal and interest payments are brought current and when future payments are reasonably assured, following a sustained period of repayment performance by the borrower in accordance with the loan's revised contractual terms.

Nonaccruing loans for all classes that are modified in a TDR are generally returned to accrual status after the borrower has made payments of cash or cash equivalents under the revised terms for at least six months subsequent to the restructuring date.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

***Premises and Equipment***

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

Costs related to computer software developed or obtained for internal use are capitalized and amortized using the straight-line method over the expected useful life (not to exceed seven years). The Company begins to amortize the software when the asset (or an identifiable component of the asset) is substantially complete and ready for its intended use.

***Fair Value***

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

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

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

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

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

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

***Goodwill and Intangible Assets***

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

The goodwill impairment analysis is a two-step test. The first step, used to identify potential impairment, involves comparing each reporting unit's fair value to its carrying value including goodwill. If the fair value

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

of a reporting unit exceeds its carrying value, applicable goodwill is deemed to be not impaired. If the carrying value exceeds fair value, there is an indication of impairment and the second step is performed to measure the amount of impairment.

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

Using a September 30 measurement date, the fair values of the Company's reporting units were determined using a combination of income and market-based approaches.

Intangible assets are generally recognized in purchase acquisitions. Core deposit intangibles, which are related to the acquired bank's deposit base, are amortized over the expected life of the related deposit base. This is generally 6 to 10 years, using primarily accelerated methods. Other customer-related intangibles are generally amortized over 8 to 10 years using accelerated methods. The Company tests intangible assets for impairment at least annually, generally at September 30.

***Bank-Owned Life Insurance***

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

***Employee Benefits***

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

***Derivatives***

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

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

During the current reporting period, the Company elected to change its accounting policy for presenting derivative assets, derivative liabilities and cash collateral on the consolidated balance sheets. This change resulted in the following presentation changes:

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

Netting derivative fair values and collateral represents a preferable method of presenting this information, as net presentation (1) allows users of the Company's financial statements to better understand the credit risk associated with our derivative portfolio, and (2) is consistent with the way the instruments are managed by the Company and therefore will provide the most relevant information to users. Prior periods have not been retrospectively adjusted as the impact of presenting derivative assets, liabilities, and cash collateral balances on a net basis is immaterial to the prior year.

***Transfers and Servicing of Financial Assets***

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

***Mortgage Banking***

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

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

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

***Income Taxes***

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

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

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

***Discontinued Operations – RBS WorldPay, Inc.***

On November 30 2010, the Company completed the sale of RBS WorldPay, Inc. in conjunction with RBSG's sale of its Global Merchant Services business. Operating results of RBS WorldPay, Inc. have been reported as discontinued operations in the consolidated financial statements for all periods presented herein; refer to Note 18 for additional information.

***New Accounting Pronouncements***

In July 2010, the FASB issued an accounting standard update which requires enhanced disclosures about the credit quality of financing receivables and the allowance for loan and lease losses. The Company elected to early adopt the expanded requirements for December 31, 2010, which are included in Notes 1, 5 and 6 to the consolidated financial statements.

In January 2010, the FASB issued an accounting standard update which enhances disclosures about fair value. New disclosures are required for (1) significant transfers in and out of Level 1 and 2 of the fair value hierarchy and (2) activity in Level 3 fair value measurements. The enhanced disclosures, included in Note 20 to the consolidated financial statements, are effective for 2010 and did not have a material impact to the consolidated financial statements.

***Revisions and Reclassifications of Prior Year Amounts***

Certain 2009 amounts have been reclassified in the consolidated financial statements and notes to conform to the current year presentation. The presentation of RBS WorldPay, Inc. as discontinued operations resulted in reclassifications to the consolidated financial statements and notes. In addition, the Company reclassified other amounts including: trading account assets (\$11 million) and current income taxes receivable (\$148 million) were combined with other assets on the consolidated balance sheet and statement of cash flows; and other leasing income (\$30 million) was split out from other income. These reclassifications had no impact to net income or to stockholder's equity.

**2. CASH AND DUE FROM BANKS**

The Company's subsidiary banks maintain certain average reserve balances and compensating balances for check clearing and other services with the FRB. The balance of deposits at the FRB amounted to \$3.6 billion and \$5.4 billion at December 31, 2010 and 2009, respectively. Average balances maintained with the FRB during the years ended December 31, 2010 and 2009 exceeded amounts required by law for the FRB's requirements. Excess amounts earned interest at the federal funds rate. As a result, the Company recorded, in interest-bearing deposits in banks, interest income on FRB deposits of \$12 million and \$13 million in 2010 and 2009, respectively.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**3. SECURITIES**

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

	December 31, 2010				December 31, 2009			
	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value	Amortized Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Value
<b><u>Available-For-Sale Securities</u></b>								
U.S. Treasury	\$577	\$0	\$0	\$577	\$95	\$0	\$0	\$95
State and political subdivisions	99	2	(1)	100	127	2	(2)	127
Other bonds, notes and debentures	1	-	-	1	4	-	-	4
Mortgage-backed securities:								
Federal agencies and U.S. government sponsored entities	16,655	502	(57)	17,100	22,424	760	(25)	23,159
Other	2,941	22	(215)	2,748	3,907	5	(487)	3,425
Total mortgage-backed securities	19,596	524	(272)	19,848	26,331	765	(512)	26,584
Total debt securities	20,273	526	(273)	20,526	26,557	767	(514)	26,810
Marketable equity securities	9	2	-	11	12	1	-	13
Other equity securities	12	-	-	12	12	-	-	12
Total equity securities	21	2	-	23	24	1	-	25
Total available-for-sale securities	\$20,294	\$528	(\$273)	\$20,549	\$26,581	\$768	(\$514)	\$26,835
<b><u>Other Investment Securities</u></b>								
Federal Reserve Bank stock	\$469	\$0	\$0	\$469	\$469	\$0	\$0	\$469
Federal Home Loan Bank stock	720	-	-	720	783	-	-	783
Venture capital and other investments	64	-	-	64	74	-	-	74
Total other investment securities	\$1,253	\$0	\$0	\$1,253	\$1,326	\$0	\$0	\$1,326



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The Company has reviewed its securities portfolio for other-than-temporary impairments. The following tables summarize those securities whose fair values are below carrying values as of December 31, 2010 and 2009 (in millions), segregated by those that have been in a continuous unrealized loss position for less than twelve months, and those that have been in a continuous unrealized loss position for twelve months or longer:

	<b>December 31, 2010</b>								
	<b>Less than 12 Months</b>			<b>12 Months or Longer</b>			<b>Total</b>		
	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>
U.S. Treasury	1	\$47	\$0	0	\$0	\$0	1	\$47	\$0
State and political subdivisions	31	32	-	3	6	(1)	34	38	(1)
Mortgage-backed securities:									
Federal agencies and U.S. government sponsored entities	39	3,057	(56)	14	396	(1)	53	3,453	(57)
Other	22	862	(46)	35	1,035	(169)	57	1,897	(215)
Total mortgage-backed securities	61	3,919	(102)	49	1,431	(170)	110	5,350	(272)
<b>Total</b>	<b>93</b>	<b>\$3,998</b>	<b>(\$102)</b>	<b>52</b>	<b>\$1,437</b>	<b>(\$171)</b>	<b>145</b>	<b>\$5,435</b>	<b>(\$273)</b>

	<b>December 31, 2009</b>								
	<b>Less than 12 Months</b>			<b>12 Months or Longer</b>			<b>Total</b>		
	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>	<b>Number of Issues</b>	<b>Fair Value</b>	<b>Gross Unrealized Losses</b>
U.S. Treasury	1	\$10	\$0	0	\$0	\$0	1	\$10	\$0
State and political subdivisions	29	41	(1)	8	12	(1)	37	53	(2)
Mortgage-backed securities:									
Federal agencies and U.S. government sponsored entities	76	2,966	(16)	20	682	(9)	96	3,648	(25)
Other	16	574	(4)	74	2,459	(483)	90	3,033	(487)
Total mortgage-backed securities	92	3,540	(20)	94	3,141	(492)	186	6,681	(512)
<b>Total</b>	<b>122</b>	<b>\$3,591</b>	<b>(\$21)</b>	<b>102</b>	<b>\$3,153</b>	<b>(\$493)</b>	<b>224</b>	<b>\$6,744</b>	<b>(\$514)</b>

For each debt security identified with an unrealized loss, the Company reviews the expected cash flows to determine if the impairment in value is temporary or other-than-temporary. If the Company has determined that the present value of the debt security's expected cash flows is less than its amortized cost basis, an other-than-temporary impairment is deemed to have occurred. The amount of impairment loss that is recognized in current period earnings is dependent on the Company's intent to sell (or not sell) the security. If the Company intends to sell the impaired security, the impairment loss recognized in current period earnings equals the difference between the instrument's fair value and its amortized cost. If the Company does not intend to sell the impaired security, and it is not likely that the Company will be required to sell the impaired security, the credit-related impairment loss is recognized in current period earnings and equals the difference between the amortized cost of the security and the present value of the expected cash flows that have currently been projected.

In addition to these cash flow projections, many other characteristics of each security are reviewed when determining whether a credit loss exists and the period over which the debt security is expected to recover. These characteristics include: (1) the type of investment, (2) various market factors affecting the fair value

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

of the security (i.e. interest rates, spread levels, liquidity in the sector, etc.), (3) the length and severity of impairment, and (4) the public credit rating of the instrument.

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

The following table presents the cumulative credit related losses recognized in earnings on debt securities held by the Company as of December 31, 2010 and December 31, 2009 (in millions):

	<b>2010</b>	<b>2009</b>
Cumulative balance through January 1	\$9	\$0
Credit impairments recognized in earnings on securities not previously impaired	13	9
Credit impairments recognized in earnings on securities that have been previously impaired	4	-
Reductions due to increases in cash flow expectations on impaired securities	(2)	-
<b>Cumulative balance through December 31</b>	<b>\$24</b>	<b>\$9</b>

Cumulative credit losses recognized in earnings for impaired debt securities held as of December 31, 2010 and 2009 were \$24 million and \$9 million, respectively. The Company recognized \$17 million and \$9 million of credit related other-than-temporary impairment losses in earnings for the years ended December 31, 2010 and 2009, respectively, related to non-agency mortgage-backed securities. No impaired debt securities were sold during 2010 or 2009. Reductions in credit losses due to increases in cash flow expectations were \$2 million for the year ended December 31, 2010 and are presented in investment securities interest income on the consolidated statement of operations. No reductions due to increased cash flows expectations were recorded in 2009. The Company does not currently have the intent to sell these securities, and it is not likely that the Company will be required to sell these securities prior to the recovery of their amortized cost bases. As of December 31, 2010 and 2009, \$147 million and \$125 million, respectively, of non-credit related other-than-temporary impairment losses were deferred in OCI.

The Company has determined that credit losses are not expected to be incurred on the remaining agency and non-agency mortgage-backed securities identified with unrealized losses as of the current reporting date. The unrealized losses on these investment securities reflect the reduced liquidity in the mortgage-backed securities market and the increased risk spreads due to the uncertainty of the United States macroeconomic environment. Therefore, the Company has determined that these securities are not other-than-temporarily impaired because the Company does not currently have the intent to sell these securities, and it is not likely that the Company will be required to sell these securities prior to the recovery of their amortized cost bases. Therefore, no impairment loss was recognized on these securities in 2010 or 2009.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The amortized cost and fair value of debt securities at December 31, 2010 by contractual maturity are shown below (in millions). Expected maturities may differ from contractual maturities because borrowers may have the right to call or prepay obligations with or without call or prepayment penalties. Contractual maturities of mortgage-backed securities are not presented because actual maturities will differ due to prepayments of the underlying mortgages.

	Amortized Cost	Fair Value
<b><u>Available-for-Sale Debt Securities</u></b>		
Due in one year or less	\$533	\$534
Due after one year through five years	31	32
Due after five years through ten years	77	77
Due after ten years	36	35
Mortgage-backed securities	19,596	19,848
<b>Total</b>	<b>\$20,273</b>	<b>\$20,526</b>

Realized gains and losses on available-for-sale securities are shown below (in millions):

	Years Ended December 31,	
	2010	2009
Gains on sale of debt securities	\$418	\$29
Losses on sale of debt securities	(5)	-
Gains on sale of marketable equity securities	6	-
<b>Total</b>	<b>\$419</b>	<b>\$29</b>

The amortized cost and fair value of securities pledged are shown below (in millions):

	December 31, 2010		December 31, 2009	
	Amortized Cost	Fair Value	Amortized Cost	Fair Value
Pledged against repurchase agreements	\$2,613	\$2,700	\$2,741	\$2,852
Pledged against Federal Home Loan Bank borrowings	320	322	1,723	1,732
Pledged against Term Auction Facility liabilities	-	-	1,256	1,240
Pledged against derivatives, to qualify for fiduciary powers, and to secure public and other deposits as required by law	6,205	6,380	7,031	7,274

As a member of the FHLB, the Company is required to hold FHLB stock. The stock can be sold only to the FHLB upon termination of membership, or redeemed at the FHLB's sole discretion.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

No loans were securitized in 2010. The Company securitized \$1.3 billion in 2009. These transactions are considered to be guaranteed mortgage securitizations, which are a form of securitization that includes a substantive guarantee by a third party. The guarantor in this case is the Federal National Mortgage Association (Fannie Mae), which purchased the underlying loans from the Company in exchange for a security backed by the loans being transferred. Because there are no proceeds, guaranteed mortgage securitizations are not considered sales of financial assets. The Company has retained the servicing rights associated with the underlying loans. These servicing rights were initially measured at fair value and will be (1) amortized into earnings over the period of estimated servicing income and (2) assessed for impairment or increased obligation on a periodic basis. The Company will have no other continuing involvement with the underlying loans transferred to Fannie Mae as part of this guaranteed mortgage securitization. The securities received from Fannie Mae are classified as available-for-sale.

**4. LOANS AND LEASES**

A summary of the loans and leases portfolio follows (in millions):

	<b>December 31,</b>	
	<b>2010</b>	<b>2009</b>
Commercial	\$21,877	\$21,253
Commercial real estate	8,920	10,463
Leases	3,016	3,290
<b>Total Commercial</b>	<b>33,813</b>	<b>35,006</b>
Home equity lines of credit	15,093	13,489
Home equity loans	8,942	12,045
Home equity products serviced by others	4,412	5,510
Residential mortgages	9,703	11,413
Automobile	8,077	8,998
Student and other installment	5,333	6,834
Credit card	1,649	1,785
<b>Total Retail</b>	<b>53,209</b>	<b>60,074</b>
<b>Total loans and leases</b>	<b>\$87,022</b>	<b>\$95,080</b>

Mortgage loans serviced for others by the Company's subsidiaries are not included above, and amounted to \$17.8 billion and \$16.3 billion at December 31, 2010 and 2009, respectively.

Loans pledged as collateral for FHLB borrowings and certain state and municipal deposits totaled \$26.0 billion and \$27.5 billion at December 31, 2010 and 2009, respectively. This collateral consisted primarily of residential mortgages and home equity loans.

Loans pledged as collateral to support borrowings at the FRB discount window totaled \$14.8 billion and \$0 at December 31, 2010 and 2009, respectively. Loans pledged as collateral to support borrowing under the Term Auction Facility ("TAF") with the FRB were \$0 and \$17.1 billion at December 31, 2010 and 2009, respectively.

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

<i>(in millions)</i>	<b>December 31,</b>	
	<b>2010</b>	<b>2009</b>
Direct financing leases	\$2,762	\$3,004
Leveraged leases	254	286
<b>Total leases</b>	<b>\$3,016</b>	<b>\$3,290</b>

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

<i>(in millions)</i>	<b>December 31,</b>	
	<b>2010</b>	<b>2009</b>
Total future minimum lease rentals	\$2,984	\$3,484
Estimated residual value of leased equipment (unguaranteed)	558	439
Initial direct costs	13	13
Unearned income on minimum lease rentals and estimated residual value of leased equipment	(539)	(646)
<b>Total leases</b>	<b>\$3,016</b>	<b>\$3,290</b>

At December 31, 2010, future minimum lease rentals on direct financing and leveraged leases are as follows (in millions):

<b>Years Ended December 31,</b>	
2011	\$562
2012	590
2013	398
2014	354
2015	261
Thereafter	819
<b>Total</b>	<b>\$2,984</b>

Pre-tax income on leveraged leases was \$6 million and \$7 million for 2010 and 2009, respectively. The income tax expense on this income was \$2 million and \$3 million for 2010 and 2009, respectively. There was no investment credit recognized in income for either year.

**5. ALLOWANCE FOR CREDIT LOSSES AND CONCENTRATIONS OF CREDIT RISK**

The allowance for loan and lease losses includes allocated reserves for the commercial and retail portfolios and unallocated reserves. Reserves for commercial and retail loans are calculated using models sensitive to historical loss rates, adjusted to reflect current economic conditions and risk characteristics. See Note 1 for a discussion of unallocated reserves.

Allocated reserves for commercial loans include a component attributable to individually impaired loans and a formula-based component for other loans and leases. Large nonaccruing loans and TDRs are assessed individually for impairment utilizing the present value of expected future cash flows, the current fair value of collateral, or the loan's observable market price. For collateral-dependent impaired loans, the excess of the Company's recorded investment in the loan over the fair value of the collateral less cost to sell is

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

charged off to the allowance for loan and lease losses. For other commercial loans assessed individually for impairment, the Company creates an impairment allowance (or adjusts an existing allowance) for the excess of the recorded investment in the loan over the expected discounted cash flows or the loan's observable market price.

For commercial loans not assessed individually for impairment and for leases, allocated reserves are developed using a formula-based methodology that considers the estimated probability of default, loss given default, and exposure at default. These factors consider the internal risk rating, loan tenor, and weighted average life.

Allocated reserves for retail loans include a component attributable to individually impaired loans identified as TDRs and a formula-based component for all other retail loans. Reserves for retail TDRs are developed using a pooled approach which considers the present value of expected future cash flows, compared to the recorded investment in the loans. The formula-based approach for retail loans is calculated at the loan level and considers the estimated probability of default, loss given default, and exposure at default. When developing these factors, the Company may consider the loan product and collateral type, loan-to-value ratio, lien position, borrower's credit, time outstanding, geographic location, and delinquency status.

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

	<b>2010</b>	<b>2009</b>
Allowance for loan and lease losses as of January 1	\$2,209	\$1,731
Charge-offs	(2,091)	(2,480)
Recoveries	242	194
Net charge-offs	(1,849)	(2,286)
Provision charged to income	1,645	2,764
Allowance for loan and lease losses as of December 31	2,005	2,209
Reserve for unfunded lending commitments as of January 1	71	52
(Credit) provision for unfunded lending commitments	(1)	19
Reserve for unfunded lending commitments as of December 31	70	71
Total allowance for credit losses as of December 31	\$2,075	\$2,280

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The recorded investment in loans and leases based on the Company's impairment methodology as of December 31, 2010 is as follows (in millions):

	<b>Commercial</b>	<b>Retail</b>	<b>Total</b>
Individually evaluated	\$974	\$615	\$1,589
Formula-based evaluation	32,839	52,594	85,433
<b>Total</b>	<b>\$33,813</b>	<b>\$53,209</b>	<b>\$87,022</b>

The following is a summary of the allowance for credit losses by impairment method as of December 31, 2010 (in millions):

	<b>Commercial</b>	<b>Retail</b>	<b>Unallocated</b>	<b>Total</b>
Individually evaluated	\$100	\$112	\$0	\$212
Formula-based evaluations	744	963	-	1,707
Unallocated	-	-	156	156
<b>Allowance for credit losses as of December 31, 2010</b>	<b>\$844</b>	<b>\$1,075</b>	<b>\$156</b>	<b>\$2,075</b>

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

The recorded investment in classes of commercial loans and leases based on regulatory classification ratings, on December 31, 2010, follows (in millions):

	<b>Pass</b>	<b>Criticized</b>			<b>Total</b>
		<b>Special Mention</b>	<b>Substandard</b>	<b>Doubtful</b>	
Commercial	\$19,774	\$916	\$806	\$381	\$21,877
Commercial real estate	6,143	1,110	818	849	8,920
Leases	2,677	261	65	13	3,016
<b>Total</b>	<b>\$28,594</b>	<b>\$2,287</b>	<b>\$1,689</b>	<b>\$1,243</b>	<b>\$33,813</b>

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The recorded investment in classes of retail loans, categorized by delinquency status, on December 31, 2010, follows (in millions):

	Residential	Home Equity Products Serviced by Others	Other Secured Retail	Unsecured Retail	Total
<u>Payment Status</u>					
Current	\$29,700	\$4,081	\$12,367	\$1,516	\$47,664
Past due fewer than 30 days	2,940	45	773	62	3,820
Past due 30 to 89 days	319	117	214	32	682
Past due 90 days or more	779	169	56	39	1,043
<b>Total balance December 31, 2010</b>	<b>\$33,738</b>	<b>\$4,412</b>	<b>\$13,410</b>	<b>\$1,649</b>	<b>\$53,209</b>

***Concentrations of Credit Risk***

Most of the Company's business activity is with customers located in New England, New York, the Mid-Atlantic States of Pennsylvania, Delaware, and New Jersey, as well as the Midwestern States of Ohio, Michigan and Illinois. Generally, loans are collateralized by assets including real estate, inventory, accounts receivable, other personal property and investment securities. As of December 31, 2010 and 2009, the Company had a significant amount of loans collateralized by residential and commercial real estate and automobiles. There are no significant concentrations to particular industries within the commercial loan portfolio. Exposure to credit losses arising from lending transactions may fluctuate with fair values of collateral supporting loans, which fail to perform according to contractual agreements. The Company's policy is to collateralize loans to the extent necessary; however, unsecured loans are also granted on the basis of the financial strength of the applicant and the facts surrounding the transaction.

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

The following table presents balances of loans with these characteristics (in millions):

	December 31, 2010					December 31, 2009				
	Residential Mortgages	Home Equity Loans & Lines of Credit	Home Equity Products Serviced by Others	Credit Cards	Total	Residential Mortgages	Home Equity Loans & Lines of Credit	Home Equity Products Serviced by Others	Credit Cards	Total
High loan-to-value	\$1,968	\$5,086	\$3,094	\$0	\$10,148	\$2,353	\$4,974	\$3,863	\$0	\$11,190
Interest only/negative amortization	774	-	-	-	774	760	-	-	-	760
Low introductory rate	-	-	-	51	51	-	-	-	122	122
Multiple characteristics & other	341	-	-	-	341	459	-	-	-	459
<b>Total</b>	<b>\$3,083</b>	<b>\$5,086</b>	<b>\$3,094</b>	<b>\$51</b>	<b>\$11,314</b>	<b>\$3,572</b>	<b>\$4,974</b>	<b>\$3,863</b>	<b>\$122</b>	<b>\$12,531</b>



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**6. NONPERFORMING ASSETS**

A summary of nonperforming loans and leases by class follows (in millions):

Nonperforming loans and leases	2010			2009		
	Nonaccruing	Accruing and 90 Days or More Delinquent	Total Nonperforming Loans and Leases	Nonaccruing	Accruing and 90 Days or More Delinquent	Total Nonperforming Loans and Leases
Commercial	\$283	\$87	\$370	\$225	\$1	\$226
Commercial real estate	927	2	929	886	65	951
Leases	13	-	13	33	-	33
<b>Total Commercial</b>	<b>1,223</b>	<b>89</b>	<b>1,312</b>	<b>1,144</b>	<b>66</b>	<b>1,210</b>
Residential	764	15	779	555	22	577
Home equity products serviced by others	169	-	169	273	-	273
Other secured retail	27	29	56	43	27	70
Unsecured retail	37	2	39	63	2	65
<b>Total Retail</b>	<b>997</b>	<b>46</b>	<b>1,043</b>	<b>934</b>	<b>51</b>	<b>985</b>
<b>Total as of December 31</b>	<b>\$2,220</b>	<b>\$135</b>	<b>\$2,355</b>	<b>\$2,078</b>	<b>\$117</b>	<b>\$2,195</b>

A summary of other nonperforming assets is as follows (in millions):

	December 31,	
	2010	2009
Other real estate owned, net of allowance:		
Commercial	\$56	\$7
Retail	62	70
<b>Total other real estate owned, net of allowance</b>	<b>\$118</b>	<b>\$77</b>

A summary of key performance indicators is as follows:

	December 31,	
	2010	2009
Nonperforming commercial loans and leases as a percentage of total loans and leases	1.51 %	1.27 %
Nonperforming retail loans as a percentage of total loans and leases	1.20	1.04
<b>Total nonperforming loans and leases as a percentage of total loans and leases</b>	<b>2.71 %</b>	<b>2.31 %</b>
	December 31,	
	2010	2009
Nonperforming commercial assets as a percentage of total assets	1.06 %	0.82 %
Nonperforming retail assets as a percentage of total assets	0.85	0.72
<b>Total nonperforming assets as a percentage of total assets</b>	<b>1.91 %</b>	<b>1.54 %</b>

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The following is an analysis of the age of the past due amounts (accruing and nonaccruing) as of December 31, 2010 (in millions):

	30-89 Days past due	90 Days or more past due	Total past due
Commercial	\$38	\$370	\$408
Commercial real estate	197	929	1,126
Leases	18	13	31
<b>Total Commercial</b>	<b>253</b>	<b>1,312</b>	<b>1,565</b>
Residential	319	779	1,098
Home equity products serviced by others	117	169	286
Other secured retail	214	56	270
Unsecured retail	32	39	71
<b>Total Retail</b>	<b>682</b>	<b>1,043</b>	<b>1,725</b>
<b>Total as of December 31</b>	<b>\$935</b>	<b>\$2,355</b>	<b>\$3,290</b>

Impaired loans include (1) nonaccruing larger balance commercial loans and (2) commercial and retail TDRs. Commercial TDRs were \$194 million and \$8 million on December 31, 2010 and 2009, respectively. Retail TDRs totaled \$615 million and \$264 million on December 31, 2010 and 2009, respectively. Commitments to lend additional funds to debtors owing receivables which were TDRs were \$0 million and \$1 million on December 31, 2010 and 2009, respectively.

A summary of impaired loan information by class follows (in millions):

	2010				2009	
	Impaired Loans With a Related Allowance	Allowance on Impaired Loans	Impaired loans Without a Related Allowance	Unpaid Contractual Balance	Total Recorded Investment in Impaired Loans	Total Recorded Investment in Impaired Loans
Commercial loans	\$222	\$45	\$68	\$380	\$290	\$229
Commercial real estate	465	55	219	1,051	684	621
<b>Total Commercial</b>	<b>687</b>	<b>100</b>	<b>287</b>	<b>1,431</b>	<b>974</b>	<b>850</b>
Residential	263	44	89	406	352	142
Home equity products serviced by others	139	57	72	221	211	92
Other secured retail	52	11	-	50	52	30
<b>Total Retail</b>	<b>454</b>	<b>112</b>	<b>161</b>	<b>677</b>	<b>615</b>	<b>264</b>
<b>Total as of December 31</b>	<b>\$1,141</b>	<b>\$212</b>	<b>\$448</b>	<b>\$2,108</b>	<b>\$1,589</b>	<b>\$1,114</b>

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**7. PREMISES AND EQUIPMENT**

A summary of the carrying value of premises and equipment follows (in millions):

	Useful Lives	December 31,	
		2010	2009
Land and land improvements	15 years	\$55	\$56
Buildings and leasehold improvements	5-20 years	646	604
Furniture, fixtures and equipment	5-10 years	1,950	1,773
Total premises and equipment, gross		2,651	2,433
Less: accumulated depreciation		1,610	1,427
Total premises and equipment from continuing operations, net		\$1,041	\$1,006
Total premises and equipment from discontinued operations, net		\$0	\$58

The above table includes capital leases with book values of \$65 million and \$51 million and related accumulated depreciation of \$37 million and \$29 million as of December 31, 2010 and 2009, respectively.

Depreciation and amortization charged to noninterest expense was \$235 million and \$250 million for the years ended December 31, 2010 and 2009, respectively.

Due to an expected change in future use, the Company evaluated several of its occupied premises for impairment as of December 31, 2010. The Company utilized third party real estate appraisers to determine the fair value of such properties and recorded a \$4 million charge to earnings as a result of the review. This charge is reported in other operating expenses in the consolidated statements of operations.

**8. LEASE COMMITMENTS**

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

At December 31, 2010, the aggregate minimum rental commitments under these non-cancelable operating leases and capital leases, exclusive of renewals, are as follows (in millions):

Years Ended December 31,	Operating Leases	Capital Leases
2011	\$189	\$10
2012	168	9
2013	143	7
2014	122	5
2015	101	2
Thereafter	312	10
Total minimum lease payments	\$1,035	\$43
Amounts representing interest	n/a	(12)
Present value of net minimum lease payments	n/a	\$31

Rental expense for such leases for the years ended December 31, 2010 and 2009 totaled \$227 million and \$219 million, respectively, and is presented in the consolidated statements of operations in equipment and occupancy expense.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**9. GOODWILL AND INTANGIBLE ASSETS**

***Goodwill***

The changes in the carrying value of goodwill for the years ended December 31, 2010 and 2009 were (in millions):

	Continuing Operations	Discontinued Operations
Balance as of January 1, 2009	\$11,709	\$0
Reclassify RBS WorldPay, Inc. to discontinued operations	(398)	398
Balance as of December 31, 2009	11,311	398
Sale of RBS WorldPay, Inc.	-	(398)
Balance as of December 31, 2010	\$11,311	\$0

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

- Retail Banking
- Commercial Banking
- Global Transaction Services – Cash Management
- Global Transaction Services – Merchant Acquiring (RBS WorldPay, Inc.)

The Company completed annual goodwill impairment tests during 2010 and 2009, using September 30 measurement dates and in accordance with the policy described in Note 1; no impairment was recorded. The fair values of the reporting units were determined using a combination of income and market-based approaches.

***Core Deposit and Other Intangibles***

A summary of the carrying value of core deposit and other intangibles follows (in millions):

	Amortizable Lives (years)	December 31, 2010			December 31, 2009		
		Gross	Accumulated Amortization	Net	Gross	Accumulated Amortization	Net
Core deposit intangibles	5 - 10	\$1,310	\$1,286	\$24	\$1,310	\$1,216	\$94
Customer relationships	8 - 10	115	103	12	115	95	20
Other	5 - 10	25	9	15	24	6	18
Total from continuing operations		\$1,450	\$1,398	\$51	\$1,449	\$1,317	\$132
Total from discontinued operations		\$0	\$0	\$0	\$121	\$95	\$26

Amortization expense during 2010 and 2009 was \$83 million and \$154 million, respectively. The portion of amortization expense related to RBS WorldPay, Inc. is reported in loss from discontinued operations and

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

was \$2 million and \$13 million in 2010 and 2009, respectively. The decrease in the amortization expense was due to normal runoff of existing intangible assets and the sale of RBS WorldPay, Inc. on November 30, 2010. The Company purchased a patent during 2010 for \$1 million dollars and reported it in other intangible assets. The Company estimates amortization expense for the next five years will be: \$31 million in 2011; \$8 million in 2012; \$4 million in 2013; \$2 million in 2014 and 2015.

**10. MORTGAGE BANKING**

In its mortgage banking business, the Company sells residential mortgage loans to government-sponsored entities and other parties, who may issue securities backed by pools of such loans. The Company retains no beneficial interests in these sales, but may retain the servicing rights of the loans sold. The Company is obligated to subsequently repurchase a loan if the purchaser, during a loan file review, discovers a standard representation or warranty violation such as noncompliance with eligibility requirements, customer fraud, or servicing violations. In addition, the Company entered into limited recourse agreements in conjunction with certain mortgage loan sales to government-sponsored entities or private parties which obligate the Company to repurchase loans in the event of default. Although these agreements provide a source of continuing exposure, the Company has not entered into any new recourse agreements since 2008. At December 31, 2010, the outstanding principal balance of loans for which the Company agreed to indemnification of potential future losses and provided specific recourse in the event of customer credit default was \$11.5 million (this approximates the maximum amount of future payments that the Company could be required to make related to such loans). As of December 31, 2010, the Company reserved \$2.0 million for estimated potential future losses associated with these recourse and indemnification agreements, based on historical loss experience. Such reserves were reported within “other liabilities” on the consolidated balance sheet.

The Company received \$4.9 billion of proceeds from the sale of residential mortgages in 2010 and 2009 and recognized gains on such sales of \$73.7 million and \$38.8 million in 2010 and 2009, respectively. Pursuant to the standard representations and warranties obligations discussed in the preceding paragraph, the Company repurchased mortgage loans totaling \$3.3 million and \$2.8 million in 2010 and 2009, respectively.

Changes related to mortgage servicing rights were as follows (in millions):

	<b>Years Ended December 31,</b>	
	<b>2010</b>	<b>2009</b>
Mortgage servicing rights:		
Balance as of January 1	\$180	\$137
Amount capitalized	71	84
Amortization	(42)	(41)
Carrying amount before valuation allowance	209	180
Valuation allowance for servicing assets:		
Balance as of January 1	1	24
Valuation impairment (recovery)	15	(23)
Balance as of December 31	16	1
Net carrying value of mortgage servicing rights as of December 31	\$193	\$179
Fair value, end of year	\$195	\$198

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

The key economic assumptions used to estimate the value of mortgage servicing rights at December 31, 2010 are presented in the following table. A sensitivity analysis as of December 31, 2010 of current fair value to an immediate 50 basis point and 100 basis point adverse change in those assumptions is also presented. These sensitivities are hypothetical. The effect of a variation in a particular assumption on the fair value of the mortgage servicing rights is calculated independently without changing any other assumption. In reality, changes in one factor may result in changes in another (for example, changes in interest rates, which drive changes in prepayment speeds, could result in changes in the discount rates), which might magnify or counteract the sensitivities. The primary risk inherent in the Company's mortgage servicing rights is an increase in prepayments of the underlying mortgage loans serviced, which is dependent upon market movements of interest rates.

<i>(Dollars in millions)</i>	<b>December 31, 2010</b>
Fair value	\$195
Weighted average life (in years)	5.0
Weighted average constant prepayment rate	14.3%
Weighted average discount rate	10.8%
Prepayment rate:	
Decline in fair value from 50 basis points adverse change	\$28
Decline in fair value from 100 basis points adverse change	\$52
Weighted average discount rate:	
Decline in fair value from 50 basis points adverse change	\$3
Decline in fair value from 100 basis points adverse change	\$6

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

	<b>December 31, 2010</b>
Weighted average life (in years)	5.0
Weighted average constant prepayment rate	15.8%
Weighted average discount rate	10.7%

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

In 2010 the Company recorded temporary impairment of \$15 million for its mortgage servicing rights, which was the result of higher prepayment rates utilized in the valuation model. The higher prepayment rates were caused by an increase in refinancing activity in 2010 due to lower mortgage rates.

Mortgage servicing fees, a component of mortgage banking income, were \$62 million and \$55 million for the years ended December 31, 2010 and 2009, respectively.

**11. DEPOSITS**

The major components of deposits are as follows (in millions):

	<b>December 31,</b>	
	<b>2010</b>	<b>2009</b>
Demand	\$19,716	\$18,994
Checking with interest	16,760	18,200
Regular savings	7,706	7,394
Money market accounts	29,696	28,127
Term deposits	18,277	25,338
<b>Total deposits</b>	<b>\$92,155</b>	<b>\$98,053</b>

Term deposits with balances greater than \$100,000 totaled \$6.4 billion as of December 31, 2010. The maturity distribution of term deposits at December 31, 2010 is as follows (in millions):

**Years Ended December 31**

2011	\$13,331
2012	2,494
2013	1,142
2014	629
2015 and thereafter	681
<b>Total</b>	<b>\$18,277</b>

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**12. BORROWED FUNDS**

The following is a summary of borrowed funds (in millions):

	December 31, 2010		December 31, 2009	
	Amount	Rate	Amount	Rate
<u>Royal Bank of Scotland Group:</u>				
Subordinated debt, due 2034, LIBOR + 1.50% with quarterly resets	\$497	1.79%	\$495	1.79%
Line of credit, \$500 available, LIBOR + .25%	-	-	188	0.42%
<u>Other borrowings:</u>				
FHLB fixed rate advances with original maturity under one year	930	0.24-0.25%	9,185	0.16-0.30%
FRB Term Auction Facility with a maturity of one month	-	-	2,000	0.25%
FHLB variable rate advances with semi-annual resets, due 2011 - 2013	5,250	0.22-0.29%	5,511	0.13-0.32%
FHLB fixed rate advances, due 2011 - 2033	140	0.00-6.60%	140	0.00-6.99%
Fixed rate senior notes, due 2011	500	5.50%	500	5.50%
Fixed rate, subordinated debt, due 2012	406	6.38%	411	6.38%
Other	61	various	78	various
<b>Total borrowed funds</b>	<b>\$7,784</b>		<b>\$18,508</b>	

Advances, lines of credit and letters of credit from the FHLB are collateralized by pledged mortgages and pledged securities at least sufficient to satisfy the collateral maintenance level established by the FHLB. The required collateral maintenance level for FHLB advances was \$7.5 billion and \$16.5 billion at December 31, 2010 and 2009, respectively. The Company's available FHLB borrowing capacity was \$6.5 billion and \$554 million at December 31, 2010 and 2009, respectively.

On March 31, 2009, the Company issued a Subordinated Floating Rate Note due April 19, 2019 in the amount of \$1.0 billion to RBSG. On August 28, 2009, the Company fully repaid and extinguished this note in exchange for the issuance of 144 shares of common stock to RBSG. This transaction resulted in no gain or loss.

In December 2009, the Company fully repaid and extinguished \$730 million of subordinated debt (due 2017-2018) to RBSG, in exchange for the issuance of 127 shares of common stock. The transaction resulted in a loss of \$1.6 million resulting from the termination of a related swap with RBSG. The swap loss is reported in the consolidated statement of operations in other net losses.



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The following is a summary of maturities for the Company's borrowed funds at December 31, 2010 (in millions):

Year	Amount
2011 or on demand	\$4,542
2012	659
2013	2,005
2014	11
2015	11
2016 and thereafter	556
<b>Total</b>	<b>\$7,784</b>

**13. PREFERRED STOCK**

The Company had authorized 30,000 shares of \$1 par value non-cumulative, non-voting perpetual preferred stock as of December 31, 2010. The preferred stock ranked senior to the common stock of the Company with respect to dividend rights upon liquidation or dissolution of the Company. The stock was not convertible into any other property of the Company, nor was it redeemable by either the Company or the holder thereof. Dividends were non-cumulative and were payable quarterly at LIBOR plus 180 basis points, if and when declared by the Company's board of directors.

In the event of any liquidation, dissolution or winding up of the Company, holders of each share of the preferred stock outstanding were entitled to be paid, out of the assets of the Company available for distribution to stockholders, before any payment is made to the holders of common stock, an amount equal to \$100,000 per share of preferred stock then issued and outstanding.

On August 28, 2009, the Company cancelled the preferences and rights of the preferred stock in its entirety. RBSG was issued 228 shares of common stock in exchange for the 15,850 preferred shares they owned. There was no gain or loss on the transaction. There were no dividends declared or paid on the preferred stock in 2009.

**14. EMPLOYEE BENEFITS**

***Pension Plans***

The Company maintains a non-contributory pension plan (the "Plan") covering substantially all employees. The Plan was frozen to new and re-hires effective January 1, 2009. Benefits under the Plan are based on employees' years of service and highest 5-year average eligible compensation. The Plan is funded on a current basis, in compliance with the requirements of the Employee Retirement Income Security Act ("ERISA"). The Company also provides an unfunded, non-qualified supplemental retirement plan.

RBSG restructured the administration of employee benefit plans during 2008. As a result, the qualified and non-qualified pension plans of certain RBSG subsidiaries (referred to as the Company's "Affiliates") merged with the Company's pension plans. As plan sponsor of the surviving plans, the Company recorded the pension asset (for the entire qualified plan) and obligation (for the entire non-qualified plan) in the accompanying consolidated balance sheets as of December 31, 2010 and 2009.

During 2010, the Company amended its defined benefit pension plans to freeze the Plan and nonqualified excess plan effective December 31, 2012. Employee service performed after December 31, 2012 will no longer accrue pension benefits. The pension asset (for the qualified plan) and obligation (for the non-qualified plan) will remain in the Company's consolidated balance sheets. The Company recorded a gain of

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

\$10 million in 2010 related to prior service costs included in accumulated other comprehensive income (“OCI”) associated with years of service no longer expected to be rendered as a result of the curtailment. The gain is presented in salaries and employee benefits in the consolidated statement of operations. During 2011 and 2012, the Company expects to recognize an additional \$2.8 million of such gains.

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

<b>Asset Category</b>	<b>Target Allocation 2011</b>	<b>2010</b>	<b>2009</b>
Equity securities	50-60 %	55.1 %	69.8 %
Debt securities	30-40 %	34.4	28.2
Other	5-15 %	10.5	2.0
<b>Total</b>		<b>100.0 %</b>	<b>100.0 %</b>

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

- Total return, consistent with prudent investment management, is the primary goal of the Plan. The nominal rate of return objective should meet or exceed the actuarial rate of return target of 8.75%. In addition, assets of the Plan shall be invested to ensure that principal is preserved and enhanced over time.
- The total return for the overall Plan shall meet or exceed the Plan’s Policy Index.
- Total portfolio risk exposure should generally rank in the mid-range of comparable funds. Risk-adjusted returns are expected to consistently rank in the top-half of comparable funds.
- Investment managers shall exceed the return of the designated benchmark index and rank in the top-half of the appropriate asset class and style universe.

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

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

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

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

The pension fund may be invested in any or all of the following asset categories:

- a) Equity-oriented investments:

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

- domestic and foreign common and preferred stocks, and related rights, warrants, convertible debentures, and other common share equivalents
  - equity index futures, and options on equity index futures
  - exchange traded options on equities
  - venture capital funds/partnerships
- b) Fixed income-oriented investments:
- domestic and foreign bonds, debentures and notes
  - mortgages
  - mortgage-backed securities
  - asset-backed securities
  - guaranteed investment contracts or certificates
  - term deposits
  - money market securities or cash
  - financial futures and options on financial futures
  - forward contracts
  - options on financial instruments

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

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

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

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

Changes in the fair value of defined benefit pension plan assets, projected benefit obligation, funded status, and accumulated benefit obligation for the years ended December 31 are summarized as follows (in millions):

	Qualified Plan		Non-Qualified Plan	
	2010	2009	2010	2009
Fair value of plan assets as of January 1	\$930	\$555	\$0	\$0
Actual return on plan assets	89	159	-	-
Employer contributions	-	150	7	7
Benefits and administrative expenses paid	(44)	(34)	(7)	(7)
Transfer in from merged plans	-	100	-	-
Fair value of plan assets as of December 31	\$975	\$930	\$0	\$0
Projected benefit obligation	\$941	\$917	\$101	\$98
Pension asset (obligation)	\$34	\$13	(\$101)	(\$98)
Accumulated benefit obligation	\$914	\$775	\$100	\$96

As of December 31, 2010, the Company's share of the pension asset (obligation) for the qualified and non-qualified plans was \$44 million and (\$99) million, respectively. There were no balances due to or due from Affiliates as of December 31, 2010. The Company recorded \$1 million and \$3 million in due from Affiliates representing the Affiliates' share of the pension assets and obligations as of December 31, 2009.

The pre-tax amounts recognized (for the qualified and non-qualified plans) in accumulated OCI as of December 31 are as follows (in millions):

	2010	2009
Net prior service credit	(\$3)	(\$33)
Net actuarial loss	342	439
Total loss recognized in accumulated other comprehensive income	\$339	\$406

Approximately \$1 million and \$20 million of prior service credit and net actuarial loss, respectively, recorded in accumulated OCI as of December 31, 2010, are expected to be recognized as components of net periodic benefit costs during 2011.

Other changes in plan assets and benefit obligations (for the qualified and non-qualified plans) recognized in OCI for the years ended December 31 include the following (in millions):

	2010	2009
Net periodic pension cost	\$42	\$69
Net actuarial loss (gain)	81	(16)
Amortization of prior service credit	2	3
Amortization of net actuarial loss	(27)	(34)
Curtailement	(123)	(3)
Transfer from merged plans	-	39
Total recognized in other comprehensive income	(67)	(11)
Total recognized in net periodic pension cost and other comprehensive income	(\$25)	\$58

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

Weighted average rates assumed in determining the actuarial present value of benefit obligations and net periodic benefit cost as of and for the years ended December 31 are as follows:

	2010	2009
<i>Assumptions for benefit obligations</i>		
Discount rate--qualified pension plan	5.75 %	6.125 %
Discount rate--non-qualified pension plan	5.63 %	6.00 %
Compensation increase rate	4.75 %	4.75 %
<i>Assumptions for net periodic pension cost</i>		
Discount rate--qualified pension plan	6.125 %	6.25 %
Discount rate--non-qualified pension plan	6.00 %	6.25 %
Compensation increases--qualified and non-qualified pension plans	4.75 %	4.00 %
Expected long-term rate of return on plan assets	8.75 %	8.75 %

The 2009 discount rate for the Affiliates' non-qualified plan net periodic cost was 6.125%. The compensation increase rate for the Affiliates' qualified and non-qualified pension plans was 4.75% for the year ended December 31, 2009.

The Company expects to contribute \$7 million to its qualified and non-qualified pension plans in 2011. The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid (in millions):

<b>Expected benefits payments by fiscal year ended</b>	
December 31, 2011	\$42
December 31, 2012	45
December 31, 2013	49
December 31, 2014	53
December 31, 2015	55
December 31, 2016 - 2020	334

***Fair Value Measurements***

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

*Money market funds, mutual funds, common stock, corporate bonds, and U.S. government agencies (collectively referred to as "securities"):*

The reported fair value is based on quoted prices, if available. Where observable quoted prices are available in an active market, securities are classified as Level 1 in the fair value hierarchy. If quoted market prices are not available, the fair value for the security is estimated by using pricing models, quoted prices of securities with similar characteristics or discounted cash flows. These instruments are classified as Level 2 because they currently trade in active markets and the inputs to the valuations are observable. The pricing models used to value securities generally begin with market prices (or rates) for similar instruments and make adjustments based on the unique characteristics of the instrument being valued. These adjustments reflect assumptions made regarding the sensitivity of each security's value to changes in interest rates and prepayments speeds. Substantially all of the plan's Level 1 and 2 securities are priced by an external pricing service.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

*Common and collective funds and other assets:*

The reported fair value is based upon information received from the investment companies. These instruments are classified as Level 3 if the underlying securities are valued using significant unobservable inputs. If the value of the underlying securities is substantially observable either from quoted prices in active markets or other observable inputs, then the fund is classified as Level 2.

The following table presents the qualified pension plan assets measured at fair value within the fair value hierarchy (in millions):

	<b>Fair Value Measurements as of December 31, 2010</b>			
	Total	Level 1	Level 2	Level 3
Cash and money market funds	\$5	\$0	\$5	\$0
U.S. government and municipal obligations	10	-	10	-
Corporate bonds	80	80	-	-
Common stock	40	40	-	-
Mutual funds	85	85	-	-
Common and collective funds	645	-	645	-
Other assets	110	-	-	110
Total assets measured at fair value	\$975	\$205	\$660	\$110

	<b>Fair Value Measurements as of December 31, 2009</b>			
	Total	Level 1	Level 2	Level 3
Cash and money market funds	\$16	\$0	\$16	\$0
U.S. government and municipal obligations	26	-	26	-
U.S. government agencies	61	-	61	-
Corporate bonds	89	89	-	-
Common stock	55	55	-	-
Mutual funds	217	217	-	-
Common and collective funds	430	-	430	-
Other assets	36	-	-	36
Total assets measured at fair value	\$930	\$361	\$533	\$36

Changes in Level 3 assets measured at fair value for the years ended December 31 are as follows:

	<b>Other assets</b>	
	<b>2010</b>	<b>2009</b>
Balance as of January 1	\$36	\$33
Increase in net gains and losses	8	2
Purchases, sales, issuances, settlements and transfers from merged plans, net	66	1
Balance as of December 31	\$110	\$36

There were no transfers between Levels 1 and 2 during the year ended December 31, 2010.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The fair values of participation units in the common and collective trusts are based on net asset value after adjustments to reflect all fund investments at fair value. The unfunded commitments, redemption frequency, and redemption notice period for the Plan investments that utilize net asset value to determine the fair value as of December 31, 2010, are as follows:

Investment	Fair Value Estimated Using Net Asset Value per Share				
	December 31, 2010				
Fair Value	Unfunded Commitment	Redemption Frequency	Other Redemption Restrictions	Redemption Notice Period	
Domestic equity funds (1)	\$78	-	Daily	None	4 days
International equity funds (2)	104	-	Monthly	None	30 days
Balanced funds (3)	372	-	Semi-monthly	None	14 days
Fixed income funds (4)	91	-	Semi-monthly	None	15 days
Total	\$645				

(1) The domestic equity fund seeks to offer participants capital appreciation by primarily investing in common stocks of companies domiciled in the United States of America. Strategies may also include total return while limiting the exposure to the equity market risk.

(2) The international equity fund seeks medium to long term capital appreciation principally through global investments in readily marketable high-quality equity securities of companies with improving fundamentals and attractive valuations.

(3) The balanced fund seeks to maximize total return by investing in global equities and fixed income transferable securities which may include some high yield fixed income transferable securities. The fund may invest in securities denominated in currencies other than U.S. dollars.

(4) The fixed income fund seeks to outperform the Barclays Capital U.S. Corporate Investment Grade Bond Index by 60 basis points over rolling three year periods.

***Postretirement Benefits***

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

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

The accumulated postretirement benefit obligation was \$31 million and \$29 million at December 31, 2010 and 2009, respectively. The funded status was a liability of \$31 million and \$29 million at December 31, 2010 and 2009, respectively and is reported in other liabilities in the accompanying consolidated balance sheets. The total cost recognized in OCI was \$4 million and \$7 million at December 31, 2010 and 2009, respectively.

The Company contributed \$2 million and \$4 million during 2010 and 2009, respectively, and paid benefits of \$2 million and \$4 million in 2010 and 2009, respectively. The benefits expected to be paid in each of the next five years is \$3 million, and \$12 million is expected to be paid during the five years from 2016 through 2020. The Company expects to contribute approximately \$3 million to the plan during 2011.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The weighted average discount rate assumed in determining the actuarial present value of benefit obligations was 5.375% and 5.75% as of December 31, 2010 and 2009, respectively.

For measurement purposes, an 8% assumed annual rate of increase in the per capita cost of covered health care benefits was used for the year ended December 31, 2010, decreasing gradually down to a 5% ultimate rate over the next several years.

***Postemployment Benefits***

The Company provides postemployment benefits to certain former and inactive employees, primarily the Company's long-term disability plan. Costs recorded for the years ended December 31, 2010 and 2009, were \$2 million.

***401(k) Plan***

The Company sponsors an employee tax-deferred 401(k) plan under which individual employee contributions to the plan are matched by the Company. Contributions are matched at 100% up to an overall limitation of 6% on a pay period basis. Employees hired or rehired on or after January 1, 2009 receive an additional 3% of earnings, subject to limits set by the Internal Revenue Service.

Amounts contributed by the Company for the years ended December 31, 2010 and 2009 were \$54 million and \$47 million, respectively.

**15. INCOME TAXES**

Total income taxes recorded for the years ended December 31, 2010 and 2009 were as follows (in millions):

	<b>Years Ended December 31,</b>	
	<b>2010</b>	<b>2009</b>
Income tax benefit on continuing operations	(\$61)	(\$420)
Income tax expense on discontinued operations	\$16	\$19
Tax effect of changes in OCI	230	699
<b>Total comprehensive income tax expense</b>	<b>\$185</b>	<b>\$298</b>

Components of income tax expense (benefit) from continuing operations are as follows (in millions):

	<b>Current</b>	<b>Deferred</b>	<b>Total</b>
<b><u>Year ended December 31, 2010</u></b>			
U.S. federal	(\$100)	\$11	(\$89)
State and local	15	13	28
<b>Total</b>	<b>(\$85)</b>	<b>\$24</b>	<b>(\$61)</b>
<b><u>Year ended December 31, 2009</u></b>			
U.S. federal	(\$384)	(\$100)	(\$484)
State and local	4	60	64
<b>Total</b>	<b>(\$380)</b>	<b>(\$40)</b>	<b>(\$420)</b>



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The effective income tax rate differed from the U.S. federal income tax rate of 35% as follows:

	<b>Years Ended December 31,</b>	
	<b>2010</b>	<b>2009</b>
Expected income tax rate	35.00 %	35.00 %
Increase (decrease) resulting from:		
State income taxes (net of federal benefit)	(37.25)	(3.51)
Uncertain tax positions	(2.51)	1.92
Life insurance	35.37	1.44
Tax-exempt interest	15.75	0.52
Low income housing partnerships	16.81	0.36
Prior year federal audit settlements	21.85	0.00
Leasing deferred tax differential	47.31	0.00
Other	(7.11)	(0.52)
<b>Effective income tax rate</b>	<b>125.22 %</b>	<b>35.21 %</b>

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities at December 31, 2010 and 2009 are presented below (in millions):

	<b>December 31,</b>	
	<b>2010</b>	<b>2009</b>
Deferred tax assets:		
Unrealized net loss on securities and derivatives	\$422	\$660
Allowance for credit losses	785	866
Accrued expenses not currently deductible	154	112
Deferred income	19	-
Net operating loss carryforwards	113	78
Investment and other tax credit carryforwards	13	12
Other	6	18
Total deferred tax assets	1,512	1,746
Valuation allowance	(168)	(141)
Deferred tax assets, net of valuation allowance	1,344	1,605
Deferred tax liabilities:		
Leasing transactions	576	592
Amortization of intangibles	435	394
Deferred income	-	36
Depreciation	6	22
Investment in subsidiaries and partnerships	-	11
Total deferred tax liabilities	1,017	1,055
Net deferred tax asset	\$327	\$550

At December 31, 2010 the Company had alternative minimum tax credits of approximately \$0.1 million, which are available to reduce future federal regular income taxes. These alternative minimum tax credits do not expire. The remaining balance of tax-deductible goodwill was \$1.2 billion and \$1.4 billion as of December 31, 2010 and 2009, respectively.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The Company had at December 31, 2010, state net operating loss and credit carry forwards of \$192 million with related deferred tax assets of \$125 million. These net operating losses and credits will expire, if not utilized, in the years 2011 through 2029.

The Company had at December 31, 2010, a valuation allowance of \$168 million against the deferred tax assets related to the state temporary differences, net operating losses and credits as it is management's current assessment that it is more likely than not that the Company will not recognize a portion of the deferred tax asset related to these items. The valuation allowance increased \$27 million during the year ended December 31, 2010.

Effective with fiscal year ended September 30, 1997, the reserve method for bad debts was no longer permitted for tax purposes. The repeal of the reserve method required the recapture of the reserve balance in excess of certain base year reserve amounts attributable to years ended prior to 1988. At December 31, 2010 the Company's base year loan loss reserves attributable to years ended prior to 1988 for which no deferred income taxes have been provided was \$557 million. This base year reserve may become taxable if certain distributions are made with respect to the stock of the Company or if the Company ceases to qualify as a bank for tax purposes. No actions are planned which would cause this reserve to become wholly or partially taxable.

The Company files income tax returns in the U.S. federal jurisdiction and various state and local jurisdictions. With few exceptions, the Company is no longer subject to U.S. federal or state and local income tax examinations by major tax authorities for years before 2000.

A reconciliation of the beginning and ending amount of unrecognized tax benefits is as follows (in millions):

	2010	2009
Balance as of January 1	\$96	\$432
Gross increases for tax positions related to prior years	16	14
Gross decreases for tax positions related to prior years	(1)	(25)
Decreases for tax positions relating to settlements with taxing authorities	(7)	(328)
Gross increases for tax positions related to the current year	-	3
<b>Balance as of December 31</b>	<b>\$104</b>	<b>\$96</b>

Included in the total amount of unrecognized tax benefits at December 31, 2010 are potential benefits of \$70 million that, if recognized, would affect the effective tax rate.

The Company classifies interest and penalties related to unrecognized tax benefits as a component of income taxes. The Company recognized \$10 million and \$8 million of interest expense in 2010 and 2009, respectively. The Company had approximately \$88 million and \$84 million accrued for the payment of interest at December 31, 2010 and 2009, respectively. There were no amounts accrued for penalties as of December 31, 2010 and 2009, and there were no penalties recognized during 2010 and 2009.

The Company anticipates settlement of a state REIT issue within the next twelve months. Settlement of this uncertainty would reduce the unrecognized tax benefit balance by \$24 million.

## 16. DERIVATIVES

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The Company's derivative instruments are recognized on the consolidated balance sheets at fair value. Information regarding the valuation methodology and inputs used to estimate the fair value of the Company's derivative instruments is described in Note 20.

The following table identifies derivative instruments included on the consolidated balance sheets in derivative assets and derivative liabilities as of December 31, 2010 and 2009 (in millions):

	2010			2009		
	Notional Amount (1)	Derivative assets	Derivative liabilities	Notional Amount (1)	Derivative assets	Derivative liabilities
Derivatives designated as hedging instruments:						
Interest rate contracts	\$10,386	\$6	\$683	\$17,186	\$0	\$1,043
Derivatives <u>not</u> designated as hedging instruments:						
Interest rate contracts	32,743	1,058	927	34,596	945	815
Foreign exchange contracts	5,189	79	75	4,264	75	64
Other contracts	1,483	25	3	1,038	13	-
Total derivatives <u>not</u> designated as hedging instruments		1,162	1,005		1,033	879
Gross derivative fair values		\$1,168	\$1,688		\$1,033	\$1,922
Less: Counterparty netting (2)		(86)	(86)		-	-
Less: Cash collateral applied (2)			(1,485)		-	-
Total derivative fair values		\$1,082	\$117		\$1,033	\$1,922

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

(2) Amounts represent the impact of legally enforceable master netting agreements that allow the Company to settle positive and negative positions and cash collateral held or placed with the same counterparties. Netting treatment was not applied to 2009 derivative assets and liabilities as the impact was not material to the balances.

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

***Institutional derivatives***

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

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

***Customer derivatives***

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

***Residential loan derivatives***

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

**Derivatives Designated as Hedging Instruments**

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

***Fair value hedges***

The Company utilizes interest rate swaps to hedge the market risk associated with various fixed income security positions. All of these swaps have been deemed as highly effective fair value hedges of the underlying securities and are marked-to-market with changes in fair value reflected in earnings (other income). The hedged securities have been classified as available-for-sale and are marked-to-market with changes in fair value reflected in OCI. The changes in fair value of the security associated with the risk being hedged (market risk) are then reclassified from OCI to earnings (other income) to offset the fair value changes of the hedging derivative.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The following table summarizes certain information related to the Company's fair value hedges for the years ended December 31, 2010 and 2009 (in millions):

	<b>The Effect of Fair Value Hedges on Net Income (Loss)</b>					
	<b>Amounts Recognized in Other Income for the Years Ended</b>					
	<b>December 31, 2010</b>			<b>December 31, 2009</b>		
	Hedged	Hedge		Hedged	Hedge	
Derivative	Item	Ineffectiveness	Derivative	Item	Ineffectiveness	
Hedges of interest rate risk on investment securities using interest rate swaps	\$11	(\$8)	\$3	\$23	(\$26)	(\$3)

***Cash flow hedges***

The Company enters into certain interest rate swap agreements designed to hedge a portion of the Company's financing liabilities (including its borrowings and deposits). All of these swaps have been deemed as highly effective cash flow hedges. The effective portion of the hedging gains and losses associated with these hedges are recorded in OCI; the ineffective portion of the hedging gains and losses is recorded in earnings (other income). Hedging gains and losses on derivative contracts reclassified from OCI to current period earnings are included in the line item in the accompanying consolidated statements of operations in which the hedged item is recorded, and in the same period that the hedged item affects earnings. During the next 12 months, approximately \$504 million of net loss (pre-tax) on derivative instruments included in OCI are expected to be reclassified to interest expense.

Hedging gains and losses associated with the Company's cash flow hedges are immediately reclassified from OCI to current period earnings (other net losses) if it becomes probable that the hedged forecasted transactions will not occur by the originally specified time period. In accordance with this policy, the Company reclassified \$321 million and \$5 million of cash flow hedging losses to current period earnings (other net losses) for the years ended December 31, 2010 and 2009, respectively.

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

	<b>The Effect of Cash Flow Hedges on Net Income (Loss) and Stockholder's Equity</b>	
	<b>Amounts Recognized for the Years Ended</b>	
	<b>December 31, 2010</b>	<b>December 31, 2009</b>
Effective portion of gain (loss) recognized in OCI (1)	(\$668)	\$68
Amounts reclassified from OCI to interest expense (2)	862	1,065
Amounts reclassified from OCI to other losses (3)	321	5

(1) The cumulative effective gains and losses on the Company's cash flow hedging activities is included on the accumulated other comprehensive loss line item on the consolidated balance sheets.

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

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

Economic Hedges

The Company's customer derivatives do not qualify for hedge accounting. These include interest rate and foreign exchange derivative contracts that are transacted to meet the hedging and financing needs of the Company's customers. Mark-to-market adjustments to the fair value of customer related interest rate contracts are included in customer derivatives in noninterest income. Mark-to-market adjustments to the fair value of foreign exchange contracts relating to foreign currency loans are included in commercial loan interest while all other foreign currency contract fair value changes are included in international fees. In both cases, the mark-to-market gains and losses associated with the customer derivatives are mitigated by the mark-to-market gains and losses on the offsetting interest rate and foreign exchange derivative contracts transacted with RBSG.

The Company's residential loan derivatives (including residential loan commitments and forward sales contracts) also do not qualify for hedge accounting. Mark-to-market adjustments to the fair value of residential loan commitments and forward sale contracts are included in noninterest income under mortgage banking.

The following table summarizes certain information related to the Company's economic hedges for the years ended December 31, 2010 and 2009 (in millions):

**The Effect of Customer Derivatives and Economic Hedges on Net Income (Loss)**

	Amounts Recognized in Noninterest Income for the Years Ended	
	2010	2009
<b><u>Customer derivative contracts</u></b>		
Customer interest rate contracts (1)	\$649	(\$70)
Customer foreign exchange contracts (2)	1	10
Residential loan commitments (3)	5	14
<b><u>Economic hedges</u></b>		
Offsetting derivatives transacted with RBSG to hedge interest rate risk on customer interest rate contracts (1)	(640)	68
Offsetting derivatives transacted with RBSG to hedge foreign exchange risk on customer foreign exchange contracts (2)	(9)	(26)
Forward sale contracts (3)	1	(9)
Total	\$7	(\$13)

(1) Reported in customer derivative income on the consolidated statements of operations.

(2) Reported in international fee income on the consolidated statements of operations.

(3) Reported in mortgage banking income on the consolidated statements of operations.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**17. COMMITMENTS, GUARANTEES AND CONTINGENCIES**

***Commitments***

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

Fund investment commitments are agreements to invest previously agreed upon amounts of capital within particular timeframes into pools of investments in start-up companies. These investments are included in other investment securities on the consolidated balance sheets.

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

During 2003, the Company entered into a 25 year agreement to acquire the naming and marketing rights of a baseball stadium in Pennsylvania. The Company paid \$3 million in 2010 and 2009 and is obligated to pay \$63 million over the remainder of the contract.

***Letters of Credit***

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

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

The Company recognizes a liability on the consolidated balance sheets representing its obligation to stand ready to perform over the term of the standby letters of credit in the event that the specified triggering events occur. The liability for these guarantees at December 31, 2010 and 2009 is \$5 million and \$7 million, respectively.

The Company determined that the payment/performance risk of the letters of credit guarantees is low. This assessment was based on an analysis of the off-balance sheet exposures attributed to regulatory risk rating categories. The Company's risk is partially mitigated by the existing collateral held.

***Risk Participation Agreements***

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

RPA's where the Company acts as the lead bank are referred to as "participations-out", in reference to the credit risk associated with the customer derivatives being transferred out of the Company. Participations-out generally occur concurrently with the sale of new customer derivatives. RPA's where the Company acts as the participating bank are referred to as "participations-in", in reference to the credit risk associated with the counterparty's derivatives being assumed by the Company. The Company's maximum credit exposure is based on its proportionate share of the settlement amount of the referenced interest rate swap. Settlement amounts are generally calculated based on the fair value of the swap plus outstanding accrued interest receivables from the customer. The Company's estimate of the credit exposure associated with its risk participations-in as of December 31, 2010 and 2009 is \$43 million and \$50 million, respectively. The current amount of credit exposure is spread out over 62 counterparties. Risk participations generally have terms ranging from 3-5 years; however certain outstanding agreements have terms as long as 15 years. There is currently a low-to-moderate probability that the Company will be required to make payment in accordance with the terms of the outstanding agreements.

***Other Guarantees***

The Company has issued a guarantee to RBSG for a fee, whereby the Company will absorb credit losses related to the sale of option contracts by RBSG to customers of the Company. There were outstanding option contracts with a notional of \$363 million and \$151 million at December 31, 2010 and 2009, respectively. For both periods, there was no liability on the balance sheet for the Company's commitment.

The following is a summary of outstanding commitments (in millions):

	December 31,	
	2010	2009
<b>Commitment amount:</b>		
Undrawn commitments to extend credit	\$43,876	\$43,313
Financial standby letters of credit	5,009	5,466
Commercial letters of credit	108	59
Performance letters of credit	83	129
Marketing rights	63	65
Fund investment commitments	16	23
Residential mortgage loans sold with recourse	12	8
Risk participation agreements	43	50

***Contingencies***

The Company has been named as a defendant in four putative class action lawsuits relating to overdraft fees charged by the Company, including the processing and posting of electronic debit transactions that result in overdraft fees charged to customers. The plaintiffs claim that overdraft fees resulting from point of sale and ATM transactions violate the duty of good faith implied in the Company's customer account agreement and constitute an unfair trade practice. Each of the four cases was transferred by the Judicial Panel on Multidistrict Litigation to a multidistrict litigation pending in the United States District Court for the Southern District of Florida, where cases relating to overdraft fees against numerous other banks had previously been transferred for pretrial proceedings.

The Company considers that it has substantial and credible legal and factual defenses to these claims and will defend them vigorously. The class action lawsuits are in very early stages, and the Company is unable to reliably estimate the liability, if any, that might arise or its effect on the Company's consolidated financial position, consolidated results of operations or consolidated cash flows in any particular period.



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The Company is involved in various other legal proceedings, all of which are incidental to the normal conduct of business. A certain amount of litigation ordinarily results from the nature of the businesses of the Company's banking and other subsidiaries. Given their complex nature, it may be years before some of these matters are ultimately resolved. Based on information currently available, the advice of legal and other counsel, and established reserves, the Company's management believes that the aggregate liabilities, if any, arising from these proceedings will not have a materially adverse effect on the Company's consolidated financial position, consolidated results of operations or consolidated cash flows.

**18. DIVESTITURES AND DISCONTINUED OPERATIONS**

***Divestitures and Discontinued Operations - 2010***

On November 30, 2010, the Company completed the sale of RBS WorldPay, Inc. in conjunction with RBSG's sale of its Global Merchant Services business.

The following amounts related to RBS WorldPay, Inc. have been segregated from the Company's continuing operations and are reported as assets or liabilities of discontinued operations on the consolidated balance sheet (in millions):

	<b>December 31, 2009</b>
<b>Assets of discontinued operations:</b>	
Cash and due from banks	\$47
Goodwill	398
Other intangibles	26
Deferred taxes, net	(17)
Premises and equipment, net	58
Other Assets	517
Total assets of discontinued operations	\$1,029
<b>Liabilities of discontinued operations:</b>	
Other liabilities	609
Total liabilities of discontinued operations	609
<b>Stockholder's equity of discontinued operations:</b>	
Additional paid-in capital	296
Retained earnings	124
Total stockholder's equity of discontinued operations	420
Total liabilities and stockholder's equity of discontinued operations	\$1,029

As a result of the sale, the Company recognized an after-tax loss of \$11 million. Net income from discontinued operations, net of taxes, excluding the loss on sale was \$10 million in 2010 and \$33 million in 2009. Pre-tax profit from discontinued operations was \$26 million in 2010 and \$52 million in 2009. Selling costs related to the sale of RBS WorldPay, Inc. of \$7 million were included in the \$11 million loss on sale in 2010 and consisted of costs allocated to the Company from RBSG.

RBS Citizens, N.A. will provide ongoing bank sponsorship to the buyer into payment networks including MasterCard and VISA. As a result, the Company will assume clearing, settlement and compliance obligations of the buyer, with indemnification of these liabilities unless the liabilities are caused by the Company. In addition, the Company will refer its customers to the buyer for payment processing services and provide cash management services to its customers. The Company forecasts that it will realize sponsorship and referral fee income of approximately \$9 million and incur sponsorship expenses of approximately \$1 million during 2011 as a result of these activities. These cash flows are expected to occur for the foreseeable future. Additionally, the Company will guarantee annual lease payments of approximately \$2.5 million through August 31, 2016 for an office building leased by the buyer.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

Prior to the sale, RBS Citizens, N.A. provided sponsorship into payment networks for RBS WorldPay, Inc. and eliminated the intercompany revenues and expenses in its consolidated financial statements. Intercompany sponsorship revenues and expenses of \$19 million and \$11 million were eliminated in 2010 and 2009, respectively.

In December 2010, the Company dissolved Charter One Reinsurance Inc., (“CORI”), a wholly-owned subsidiary which provided mortgage insurance through agreements with several private mortgage insurers. In conjunction with the dissolution, CORI transferred all future risk and reinsurance obligations by commuting their reinsurance agreements to the private mortgage insurers.

***Divestitures – 2009***

On March 20, 2009 the Company completed the sale of 65 branches in Indiana. Assets and deposits totaled \$49 million and \$424 million, respectively. A gain of \$8 million was recognized in other net losses.

**19. RELATED PARTY TRANSACTIONS**

The following is a summary of funds borrowed from RBSG (in millions):

	<b>Interest Rate</b>	<b>Maturity Date</b>	<b>December 31,</b>	
			<b>2010</b>	<b>2009</b>
<b>Subordinated debt</b>	Three month LIBOR + 1.50%	March 2034	\$497	\$495
<b>Revolving line of credit</b>	Overnight LIBOR + .25%	-	-	\$188
<b>Term federal funds purchased</b>	.26% in 2009	-	-	\$1,000

In December 2009, the Company fully repaid and extinguished \$730 million of Subordinated Debt (due 2017-2018) to RBSG, in exchange for the issuance of 127 shares of common stock. The transaction resulted in a loss of \$1.6 million resulting from the termination of a related swap with RBSG.

On August 28, 2009, the Company cancelled the preferences and rights of the preferred stock in its entirety. RBSG was issued 228 shares of common stock in exchange for their 15,850 preferred shares. There was no gain or loss on the transaction.

On March 31, 2009, the Company issued a Subordinated Floating Rate Note due April 19, 2019 in the amount of \$1.0 billion to RBSG. On August 28, 2009, the Company fully repaid and extinguished this note in exchange for the issuance of 144 shares of common stock to RBSG. This transaction resulted in no gain or loss.

The Company enters into interest rate swap agreements with RBSG for the purpose of reducing the Company’s exposure to interest rate fluctuations. As of December 31, 2010, the total notional amount of swaps outstanding was \$10.4 billion which pay fixed rates ranging from 1.24% to 5.47% and receive one or three month LIBOR or overnight fed funds rate with maturities from 2011 through 2017. As of December 31, 2009, the total notional amount of swaps outstanding was \$17.2 billion which pay fixed rates ranging from 1.94% to 5.54% and receive one or three month LIBOR with maturities from 2010 through 2016.

In order to meet the financing needs of its customers, the Company enters into interest rate swap and cap agreements with its customers and simultaneously enters into offsetting swap and cap agreements with RBSG. The Company earns a spread equal to the difference between rates charged to the customer and rates charged by RBSG. The notional amount of these interest rate swap and cap agreements outstanding with RBSG was \$16.3 billion and \$17.4 billion at December 31, 2010 and 2009, respectively.

Also to meet the financing needs of its customers, the Company enters into a variety of foreign currency denominated products, such as loans, deposits and foreign exchange contracts. To manage the foreign

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

exchange risk associated with these products, the Company simultaneously enters into offsetting foreign exchange contracts with RBSG. The Company earns a spread equal to the difference between rates charged to the customer and rates charged by RBSG. The notional amount of foreign exchange contracts outstanding with RBSG was \$3.0 billion and \$2.6 billion at December 31, 2010 and 2009, respectively.

Net expense paid to RBSG for the years ended 2010 and 2009 totaled \$1.4 billion and \$1.8 billion, respectively. The decreased expense over the prior year related primarily to the amortization of discontinued hedges (\$250 million) and lower interest rates.

The Company receives income for providing services and referring customers to RBSG. The total fee income received in 2010 and 2009 was \$22 million and \$20 million, respectively.

The Company, as a matter of policy and during the ordinary course of business with underwriting terms similar to those offered to the public, has made loans to directors and executive officers and their immediate families, as well as their affiliated companies. Such loans amounted to \$84 million and \$85 million at December 31, 2010 and 2009, respectively.

**20. FAIR VALUE MEASUREMENTS**

As discussed in Note 1, the Company measures or monitors many of its assets and liabilities on a fair value basis. Fair value is used on a recurring basis for assets and liabilities for which fair value is the required or elected basis of accounting. Additionally, fair value is used on a nonrecurring basis to evaluate assets for impairment or for disclosure purposes. Nonrecurring fair value adjustments typically involve the application of lower of cost or market accounting or write-downs of individual assets.

The Company also applies the fair value measurement guidance to determine amounts reported for certain disclosures in this note for assets and liabilities not required to be reported at fair value in the financial statements.

***Fair Value Option, Residential Loans Held-for-Sale***

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

The fair value of residential loans held-for-sale is derived from observable mortgage security prices and includes adjustments for loan servicing value, agency guarantee fees, and other loan level attributes which are mostly observable in the marketplace. Credit risk is not material to the valuation since the loans are sold shortly after origination. Therefore, the Company classifies the residential loans held-for-sale in Level 2 of the fair value hierarchy.

At December 31, 2010, the fair value carrying amount of residential loans held-for-sale and the aggregate unpaid principal amount that the Company is contractually entitled to receive at maturity are \$716 million and \$711 million, respectively. At December 31, 2009 the fair value carrying amount of residential loans held-for-sale and the aggregate unpaid principal amount that the Company is contractually entitled to receive at maturity were \$456 million and \$451 million, respectively. The amount of loans past due or nonaccruing is not material.

The loans accounted for under the fair value option are initially measured at fair value when the financial asset is recognized. Subsequent changes in fair value are recognized in current earnings. The Company recognized a \$0.5 million decrease and \$0.7 million increase in mortgage banking noninterest income for the years ended December 31, 2010 and 2009, respectively. Interest income on residential loans held-for-sale is calculated based on the note rate of the loan and is recorded in interest income. Changes in fair value of the residential mortgages held for sale due to instrument-specific credit risk during the years ended December 31, 2010 and 2009 were not material.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

***Recurring Fair Value Measurements***

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

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

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

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

Residential loans held for sale: See the Fair Value Option discussion above.

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

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The following table presents assets and liabilities measured at fair value on a recurring basis (in millions):

	<b>December 31, 2010</b>			
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Securities available-for-sale:				
Equity securities	\$23	\$10	\$13	\$0
U.S. Treasury	577	577	-	-
State and political subdivisions	100	-	100	-
Mortgage-backed securities	19,848	-	19,848	-
Other debt securities	1	-	1	-
Residential loans held for sale	716	-	716	-
Derivative assets:				
Interest rate contracts - hedged instruments	6	-	6	-
Interest rate contracts - non hedged instruments	1,058	-	1,058	-
Foreign exchange contracts - non hedged instruments	79	-	79	-
Other contracts - non hedged instruments	25	-	25	-
Venture capital investments	64	-	-	64
<b>Total assets</b>	<b>\$22,497</b>	<b>\$587</b>	<b>\$21,846</b>	<b>\$64</b>
<b>Liabilities</b>				
Derivative liabilities:				
Interest rate contracts - hedged instruments	\$683	\$0	\$683	\$0
Interest rate contracts - non hedged instruments	927	-	927	-
Foreign exchange contracts - non hedged instruments	75	-	75	-
Other contracts - non hedged instruments	3	-	3	-
<b>Total liabilities</b>	<b>\$1,688</b>	<b>\$0</b>	<b>\$1,688</b>	<b>\$0</b>
<b>December 31, 2009</b>				
	Total	Level 1	Level 2	Level 3
<b>Assets</b>				
Securities available-for-sale:				
Equity securities	\$25	\$8	\$17	\$0
U.S. Treasury	95	95	-	-
State and political subdivisions	127	-	127	-
Mortgage-backed securities	26,584	-	26,584	-
Other debt securities	4	-	4	-
Residential loans held for sale	456	-	456	-
Derivative assets:				
Interest rate contracts - non hedged instruments	945	-	945	-
Foreign exchange contracts - non hedged instruments	75	-	75	-
Other contracts - non hedged instruments	13	-	13	-
Venture capital investments	74	-	-	74
<b>Total assets</b>	<b>\$28,398</b>	<b>\$103</b>	<b>\$28,221</b>	<b>\$74</b>
<b>Liabilities</b>				
Derivative liabilities:				
Interest rate contracts - hedged instruments	\$1,043	\$0	\$1,043	\$0
Interest rate contracts - non hedged instruments	815	-	815	-
Foreign exchange contracts - non hedged instruments	64	-	64	-
<b>Total liabilities</b>	<b>\$1,922</b>	<b>\$0</b>	<b>\$1,922</b>	<b>\$0</b>

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The changes in Level 3 assets measured at fair value on a recurring basis are summarized as follows for the years ended December 31, 2010 and 2009 (in millions):

	<b>2010</b>	<b>2009</b>
Balance as of January 1	\$74	\$90
Purchases, sales, issuances, settlements (net)	1	(1)
Net transfers into Level 2	-	-
Other net losses	(11)	(15)
Balance as of December 31	<u>\$64</u>	<u>\$74</u>
Net unrealized gains (losses) included in net income for the year relating to assets held at December 31	<u>\$3</u>	<u>(\$14)</u>

There were no transfers between Levels 1 and 2 during the year ended December 31, 2010.

***Nonrecurring Fair Value Measurements***

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

Impaired Loans: The carrying amount of collateral-dependant impaired loans is compared to the appraised value of the collateral. Any excess of carrying amount over the appraised value is charged to the allowance for loan and lease losses.

Credit card receivables: The fair value of credit card receivables is based on observable market-based inputs.

MSRs: Mortgage servicing rights do not trade in an active market with readily observable prices. Therefore, the Company determines the fair value of mortgage servicing rights using a model that calculates the present value of estimated net future servicing income. The model utilizes assumptions that market participants use in estimating future net servicing income, including estimates of prepayment speeds, default rates, cost to service, discount rate, escrow earnings, contractual servicing fee income, and ancillary income. The discount rate is the required rate of return investors in the market would expect for an asset of similar risk. Mortgage servicing rights are classified as Level 3 since the valuation methodology utilizes significant unobservable inputs.

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

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

	Carrying Value at December 31, 2010				Year Ended December 31, 2010
					Total Losses
	Total	Level 1	Level 2	Level 3	
Impaired collateral dependent loans (1)	\$519	\$0	\$519	\$0	(\$298)
MSRs (3)	193	-	-	193	(15)
Foreclosed assets (4)	114	-	114	-	(6)

  

	Carrying Value at December 31, 2009				Year Ended December 31, 2009
					Total Gains (Losses)
	Total	Level 1	Level 2	Level 3	
Impaired collateral dependent loans (1)	\$589	\$0	\$589	\$0	(\$315)
Credit card receivables (2)	518	-	518	-	(55)
MSRs (3)	179	-	-	179	23
Foreclosed assets (4)	56	-	56	-	(11)

(1) In 2010, impaired loans for which collection is dependent on the loan's collateral in the amount of \$803 million were written down to \$519 million resulting in an impairment charge of \$298 million, which was charged to the allowance for loan and lease losses. In 2009, impaired loans for which collection is dependent on the loan's collateral in the amount of \$981 million were written down to their fair value of \$589 million resulting in an impairment charge of \$315 million, which was charged to the allowance for loan and lease losses. Fair value of the loans was based on the appraised value of the collateral.

(2) In December 2009, credit card receivables totaling \$573 million were transferred to loans held-for-sale and written down to their fair value of \$518 million. The write-down reduced the allowance for loan and lease losses by \$55 million and increased loan loss provision by \$17 million.

(3) In 2010, MSRs totaling \$208 million were evaluated for impairment and written down to \$193 million, resulting in an impairment charge of \$15 million. In 2009, MSRs totaling \$156 million were revalued to \$179 million which resulted in a \$23 million reversal of impairment previously recorded.

(4) In 2010, foreclosed real estate accounted for at the lower of cost or fair value less costs to sell was written down to fair value of \$114 million, resulting in impairment charges of \$6 million. In 2009, foreclosed real estate accounted for at the lower of cost or fair value less costs to sell was written down to fair value of \$56 million, resulting in impairment charges of \$11 million.

***Disclosures about Fair Value of Financial Instruments***

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

Loans and leases: For loans and leases not recorded at fair value on a recurring basis, fair value is estimated by discounting the expected future cash flows using current rates which a market participant would likely use to value similar pools of loans. The internal risk weighted balances of loans are grouped by product type for purposes of this estimated valuation. For non-accruing loans, fair value is estimated by discounting management's estimate of future cash flows with a discount rate commensurate with the risk associated with such assets.



**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

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

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

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

The following table is a summary of fair value for financial instruments not recorded at fair value in the consolidated financial statements. The table excludes instruments that re-price within 90 days, for which carrying amounts approximate fair value, and financial instruments recorded at fair value on a recurring basis. The carrying amounts in the following table are recorded in the consolidated balance sheets under the indicated captions (in millions):

	December 31, 2010		December 31, 2009	
	Carrying Value	Fair Value	Carrying Value	Fair Value
<b><i>Financial Assets:</i></b>				
Loans and leases	\$87,022	\$81,783	\$95,080	\$87,138
Other investment securities	1,253	1,253	1,326	1,326
<b><i>Financial Liabilities:</i></b>				
Deposits	92,155	92,270	98,053	98,223
Federal funds purchased and securities sold under agreement to repurchase	5,112	5,112	5,222	5,222
Borrowed funds	7,784	7,758	18,508	18,542

**21. REGULATORY MATTERS**

As a bank holding company, the Company is subject to regulation by the Office of the Comptroller of the Currency ("OCC"), Federal Reserve and the Federal Deposit Insurance Corporation ("FDIC"), as well as state regulators. Under the regulatory capital adequacy guidelines of the Federal Deposit Insurance Corporation Improvement Act of 1991 ("FDICIA"), the Company and its banking subsidiaries must meet specific capital requirements. These requirements are expressed in terms of the following ratios: (1) Risk-based Total Capital (total capital/risk-weighted on-and off-balance sheet assets); (2) Risk-based Tier 1 Capital (tier 1 capital/risk weighted on- and off-balance sheet assets); and Tier 1 Leverage (tier 1 capital/adjusted average quarterly assets). To meet the regulatory capital requirements, the Company and its banking subsidiaries must maintain minimum Risk-based Total Capital, Risk-based Tier 1 Capital, and Tier 1 Leverage ratios. In addition, the Company must not be subject to a written agreement, order or capital directive with any of its regulators. Failure to meet minimum capital requirements can result in the initiation of certain actions that, if undertaken, could have a material effect on the Company's consolidated financial statements.

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

The following table presents capital and capital ratio information for the Company as of December 31, 2010 and 2009 (dollars in millions):

	<b>FDIC Requirements</b>					
	<b>Actual</b>		<b>Minimum Capital Adequacy</b>		<b>Classification as Well-capitalized</b>	
	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>	<b>Amount</b>	<b>Ratio</b>
<i>As of December 31, 2010</i>						
Total Capital to Risk Weighted Assets	\$13,816	14.39%	7,682	8.00%	\$9,602	10.00%
Tier 1 Capital to Risk Weighted Assets	12,524	13.04%	3,841	4.00%	5,761	6.00%
Tier 1 Capital to Average Assets	12,524	10.44%	3,599	3.00%	5,998	5.00%
<i>As of December 31, 2009</i>						
Total Capital to Risk Weighted Assets	\$13,555	13.03%	\$8,320	8.00%	\$10,400	10.00%
Tier 1 Capital to Risk Weighted Assets	12,083	11.62%	4,160	4.00%	6,240	6.00%
Tier 1 Capital to Average Assets	12,083	8.68%	4,174	3.00%	6,957	5.00%

In accordance with Federal and state banking regulations, dividends paid by the Company's banking subsidiaries to the Company itself are generally limited to the retained earnings of the respective banks.

There were no common stock dividends in 2010 and 2009.

In November 2009, the FDIC approved a rule that required all banks to prepay the estimated FDIC assessments for 2010, 2011, and 2012. The balance in the prepaid assessment was \$465 million and \$588 million as of December 31, 2010 and 2009, respectively.

## 22. SUPPLEMENTAL INFORMATION

Supplemental cash flow information and non-cash activities are as follows (in millions):

	<b>Years Ended December 31,</b>	
	<b>2010</b>	<b>2009</b>
<b>Supplemental cash flow information:</b>		
Interest paid	\$1,391	\$2,508
Income taxes refunded	(258)	(177)
<b>Supplemental schedule of noncash investing and financing activities:</b>		
Loans securitized and transferred to securities available-for-sale	\$0	\$1,271
Credit card loans transferred from portfolio to held for sale	-	518
Additional common stock issued after cancellation of preferred stock	-	1,585
Conversion of subordinated debt to common stock	-	1,730
Due to broker for securities purchased but not settled	693	-

**CITIZENS FINANCIAL GROUP, INC.**  
**NOTES TO CONSOLIDATED FINANCIAL STATEMENTS**  
**As of and for Years Ended December 31, 2010 and 2009**

**23. EXIT COSTS AND RESTRUCTURING RESERVES**

In 2010, the Company reviewed its structural expense base in a Company-wide effort to create a more streamlined organization, reduce expense growth, and provide investment funds for future growth initiatives.

In 2009, the Company announced a restructuring plan based on a strategic review of its technology infrastructure. The plan involves aligning the technology infrastructure across geographies and business divisions and will reduce the workforce by approximately 1,250 over the next two years.

In the year ended December 31, 2010, the Company recorded a \$55 million charge to noninterest expense for other restructuring charges consisting primarily of employee termination benefits of \$14 million, lease termination costs of \$12 million, building impairment of \$14 million, and miscellaneous divestiture costs of \$10 million. In 2009, the Company recorded a \$65 million charge to noninterest expense, consisting primarily of employee termination benefits of \$42 million and lease termination costs of \$18 million.

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

	<b>Severance</b>	<b>Facilities Costs</b>	<b>Fixed Assets</b>	<b>Contract Termination</b>	<b>Other</b>	<b>Total</b>
Reserve balance as of January 1, 2009	\$0	\$0	\$34	\$4	\$0	\$38
Additions	42	20	-	-	3	65
Utilization	(36)	(4)	(34)	(4)	(3)	(81)
Reserve balance as of December 31, 2009	\$6	\$16	\$0	\$0	\$0	\$22
Additions	14	26	-	-	15	55
Utilization	(11)	(27)	-	-	(14)	(52)
Reserve balance as of December 31, 2010	\$9	\$15	\$0	\$0	\$1	\$25

**24. SUBSEQUENT EVENTS**

The Company has evaluated events that have occurred subsequent to December 31, 2010 through February 22, 2011, the date the consolidated financial statements were issued. The Company is not aware of any subsequent events which would require recognition or disclosure in the consolidated financial statements.