Shawbrook Bank Limited

Annual Report and Accounts

For the Year Ended 31 December 2017

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A full version of our Annual Report and Pillar 3 Report are available online at www.shawbrook.co.uk

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Company information

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Robin Ashton
David Gagie
Cédric Dubourdieu
Sally-Ann Hibberd
Roger Lovering
Lindsey McMurray
Paul Lawrence
Andrew Didham

Executive Directors

Steve Pateman
Dylan Minto

Company Secretary

Daniel Rushbrook

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Company number: 388466

Chairman's statement
Iain Cornish

I am delighted to introduce this year's Annual Report & Accounts, in what has been another successful year for the Group in 2017, with continued growth across the business.

The Group has achieved a strong performance, with underlying profit before tax of £106 million and an underlying return on tangible equity of 19.9%. We are confident that our clear and consistent strategy and the disciplined implementation of our business model will ensure we continue to support our clients and generate good returns even in a more uncertain environment.

Accelerating our strategy
Clearly a significant event in 2017 has been the Board's decision ultimately to accept a bid from the Marlin consortium (a private equity consortium of Pollen Street Capital and BC Partners). Throughout the offer process the Board considered the interests of the independent shareholders and other stakeholders at every phase, and notwithstanding the significant time consumed by this, the Executive management team did a tremendous job in continuing to keep focussed on the progression of the business.

Commitment to strong Governance
The Board's responsibility to provide strong and effective governance remains paramount. Throughout 2017 we aligned to the provisions included within UK Corporate Governance Code (the 'Code') as detailed within the Corporate Governance Report. We remain committed to strong governance standards and we have worked closely with our new shareholder to ensure that the Board can operate independently and continue to protect the interests of all stakeholders.

During 2017, the Board welcomed the appointment of Andrew Didham, Independent Non-Executive Director and Chairman of the Audit Committee, Cédric Dubourdieu, Non-Executive Director and Dylan Minto as Chief Financial Officer. I believe the Board is well placed to provide effective oversight of the Group in the delivery of its strategy.

Our communities
We remain committed to investing in the communities we are a part of, whether that is within Shawbrook through development of our people; our local communities through volunteering and fundraising; or the broader UK economy through lending to businesses, landlords, house builders or personal customers. We are also committed to strong corporate responsibility.

Outlook
I am highly confident in the capability of the Group, with an Executive Management team with strength and depth, and the excellence of colleagues throughout the business to continue delivering growth and value into the future. During the year I took the decision that with the change in ownership it was an appropriate time to step down. Finally, I would like to express my gratitude to all my colleagues over the last three years for the continual support they have given to me and to the Group.

Iain Cornish
Chairman

Chief Executive Officer's statement
Steve Pateman

OPPORTUNITY

2017 was another year of considerable progress for Shawbrook and one of great change with the company accepting a bid from the Marlin Consortium valuing the company at c.£850m in July and de-listing its securities in August.

The change in ownership creates a stable and supportive shareholder base upon which to build a medium term plan to develop our existing business recognising the opportunities and challenges that will arise from the pace of technological change and how this impacts both our traditional distribution and servicing methodologies as well as the ongoing changes within the banking market as the mainstream banks refine their risk appetite, capital planning in preparation for Basel 4 and distribution leaving many business and personal customers looking for banking providers that have a more accommodating risk appetite.

Shawbrook was created to serve customer markets with an adjacent risk profile to the mainstream providers but to do so with thoughtful and considered underwriting rather than rely purely on scorecards, models and algorithims, all of which have a part to play in an effective risk management model; our approach to risk management was once again a core strength with our underlying cost of risk at 0.53% on a customer loan book which grew 20% to £4.9bn.

Our markets continued to be challenging reflecting the impact of high liquidity on both competitive pricing and risk appetite; by maintaining an appropriate discipline we were able to hold our NIM at 5.4% offsetting margin compression by improving funding costs.

Our Property business grew 27% to £3.2bn albeit adversely impacted in the final quarter by changes to our underwriting criteria in second charge mortgages; Consumer grew 33% to £0.6bn as our Personal and Retail Finance franchises gathered momentum whilst maintaining origination levels in our maturing Home Improvement and Holiday Ownership businesses. Business Finance held flat at £1.1bn and remained a highly competitive market whilst the Regional Business Centres continued to establish themselves, Specialist Asset Finance had a record year and was offset by a high level of redemption in Wholesale Finance where pricing has moved outside our return criteria.

We continued to bring new products to the market with the launch of the Motor Flexiloan in Consumer in partnership with the RAC, expansion of our first charge mortgage business into more complex mortgage products and the introduction of further specialist asset classes in Asset Finance, agriculture and renewables. Our Jersey business continued to grow and in December we completed the acquisition of the Royal Bank of Scotland International offshore portfolio in partnership with Investec. We have now staffed and opened seven Regional Business Centres and these will also house our growing Development Finance business which from a standing start in 2017 now has committed facilities of c.£110m. We also successfully adapted our buy-to-let business to the revised underwriting regulatory standards introduced in September.

Profitability was impacted by the one-off costs incurred on the change in ownership and on an underlying basis was up 19.5%; whilst the outlook for the economy is challenging reflecting the uncertainty around how the UK will exit the European Union and we would expect price and risk competition to remain intense, we believe that our product diversity will allow us to maintain our levels of organic growth and there will continue to be modest inorganic opportunities. Accordingly, we took the opportunity in December to strengthen our capital base with the successful issue of £125m of Additional Tier 1 securities.

Our strong income growth has allowed us to continue to invest in the franchise with headcount increasing to 671 (2016: 569). Our underlying cost to income ratio increased to 45.7% as we invested for the future and continue to plan to reduce this further to 35% by 2020, notwithstanding the investment required to maintain and enhance our IT architecture. The strong disciplines applied to capital allocation, underwriting and investment allowed us to deliver a RoTE of 19.9%, however we are carrying surplus levels of capital to support growth with a Total Capital Ratio of 19.1% and continue to target RoTE in the range of 22-25%.

I would like to close by thanking my colleagues for their contribution to the business over the last 12 months, to the Board for their continued support and to Iain Cornish whose counsel I will miss when he passes on the role of Chairman to his successor . Iain has guided the Group through a challenging period following the Initial Public Offering in April 2015 and it is appropriate to thank him for his contribution to the significant progress we have made in building the banking business we have today.

Steve Pateman
Chief Executive Officer

Stratrategic Report

How we've done
2017 key highlights

How we have delivered against our strategic pillars

Achieve strong risk-adjusted returns	5.4% Stable NIM throughout 2017	
Maintain excellent credit quality	53bps Cost of risk	
Progressively increase orginations	20% Increase in loan book to £4.9bn	
Maintain conservative foundations	12.8% CET1 ratio	19.1% Total Capital Ratio
Enhance customer focus	89% *Customer satisfaction* (As conducted in our 2017 Charterhouse survey)	

Strategic Report (continued)

Our Business

What we do

Shawbrook is a specialist UK lending and savings bank focused on Property Finance, Business Finance and Consumer lending and savings. We differentiate ourselves by concentrating on markets where our specialist knowledge, judgement and personalised approach to underwriting offers us a competitive advantage. This supports attractive, stable returns and sustainable growth, and also benefits businesses and consumers in parts of the market which continue to be poorly served by mainstream banks.

Our divisions

Property Finance

The Property Finance Division has a well-diversified product range with both residential and commercial mortgage offerings.

£3.2bn

Customer loans

Business Finance

The Business Finance Division offers an extensive product range, enabling it to provide a comprehensive suite of services to address the needs of the UK SME market.

£1.1bn

Customer loans

Consumer

The Consumer Division offers a broad range of lending and savings products enabling it to provide unsecured loans to consumers for a variety of purposes in addition to a range of savings products.

£0.6bn

Customer loans

Strategic Report (continued)

Our people and community

671

Employees
(period average)

52

Charities
supported

58% M 42% F

Gender split

Our five strategic pillars

Achieve strong risk adjusted returns

Maintain excellent credit quality

Progressively increase originaations

Maintain conservative foundations

Enhance customer focus

Strategic Report (continued)

Our Strategy

Our five strategic pillars	How we will achieve these
Achieve strong risk adjusted returns	Continue to identify specialist lending sectors Achieve strong returns whilst maintaining high quality underwriting standards
Maintain excellent credit quality	Ensure that the loan book is sustainable over the long term when markets may not be so benign
Progressively increase originations	Increase organic originations Continue to identify and carefully enter adjacent specialist markets Further increase diversification
Maintain conservative foundations	Conservative approach to risk management Prudently positioned capital, funding and liquidity
Enhance customer focus	The SME Champion – we meet the needs of poorly served markets Consumer specialists – we serve sectors where our products and high degree of choice differentiate our offer Exploit leading edge technology to enhance customer experience and drive efficiencies

Risk management

Key risk categories

The key risk categories faced by the Group are as follows:

Risk Category	Definition
Credit Risk (including concentration and single name risk)	• The risk that a borrowing client or treasury counterparty fails to repay some or all of the capital or interest advanced to them. This category also includes Credit Concentration risk which is the risk of exposure to particular groups of customers or sectors or geographies that uncontrolled may lead to additional losses that its shareholders or the market may not expect.
Liquidity and Market Risk	• Liquidity Risk is the risk that the group is unable to meet its current and future financial obligations as they fall due, or is only able to do so at excessive cost. • Market Risk is the risk of financial loss through un-hedged or mismatched asset and liability positions that are sensitive to changes in interest rates or currencies.
Operational Risk	• Operational Risk is the risk of loss resulting from inadequate or failed internal processes, people and system failures, or from external events including strategy and reputational risks.
Conduct, Legal and Compliance Risk	• Conduct Risk is the risk that the Group's behaviour will result in poor customer outcomes and that our people fail to behave with integrity. • Legal and Compliance Risk is the risk of regulatory enforcement and sanction, material financial loss, or loss to reputation the Group may suffer as a result of its failure to identify and comply with applicable laws, regulations, codes of conduct and standards of good practice.
Strategic Risk	• Risk that the Group is unable to meet its objectives through the inappropriate selection or implementation of strategic plans. This includes the ability to generate lending volumes inside risk appetite.
Systems and Change Risk	• Systems and change risk is the risk that transition changes in the business will be improperly implemented.

Risk management (continued)

A more detailed summary of each principal risk is contained in the following sections.

Credit Risk

This risk has two main components:

- Customer risk (from core lending activity); and
- Treasury credit risk (from treasury activity).

The Group's Treasury Credit Risk exposure is limited to short term deposits placed with leading UK banks.

Credit Risk Approval Process

The Group operates a hierarchy of lending authorities based principally upon the size of the aggregated credit risk exposure to counterparties, group of connected counterparties or, where applicable, a portfolio of lending assets that are subject to a single transaction. In addition to maximum amounts of credit exposure, sole lending mandates may stipulate sub-limits and / or further conditions and criteria.

The Group implemented a number of changes to its hierarchy of lending mandates during 2016. Each Division has a maximum authority level allocated, with exposures above these levels requiring approval from an approver in the Second Line of Defence or the Credit Approval Committee. In each Lending Division, at least one signatory to the loan must be a segregated First Line of Defence Credit Approver who has no responsibility for, or remuneration arrangements linked to, sales targets, on-going sales origination or relationship responsibility with the borrower.

The maximum Divisional mandate for Business Finance Regions, Business Finance Specialist Sectors and commercial property in the Property Division is £1.25m. The maximum Divisional mandate for secured lending in the Property Division is £100k and £75k in Consumer. Exposures beyond these limits up to £5m may be approved by an approver in the Second Line of Defence and exposures up to the Group single name concentration limit of £25m must be approved by the Credit Approval Committee. In addition, where transactions involve financing portfolios of lending assets in excess of £15m or where an individual loan is required in excess of £25m Board approval is also required.

Lending is advanced subject to Group lending approval policy and specific credit criteria. When evaluating the credit quality and covenant of the borrower, significant emphasis is placed on the nature of the underlying collateral. This process also includes the review of the Board's appetite for concentration risk.

Credit Monitoring

Approval and on-going monitoring control is exercised both within the businesses and through oversight by the Group Credit Risk function. This applies to both individual transactions as well as at the portfolio level by way of monthly credit information reporting, measurement against Risk Appetite limits and testing via risk quality assurance reviews.

The Divisions operate timely collections and arrears management processes. The Group further invested in 2017 in developing its operational arrangements and capabilities for non-performing loan management to ensure that the Group is capable of operating in a more challenging environment where interest rates are rising and there is lower demand and liquidity in property markets.

Liquidity and Market Risk

Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due, or is only able to do so at excessive cost.

Market risk is the risk associated with adverse changes in the fair value of positions held by the Group as a result of movement in market factors such as interest rates, currencies, volatility and credit spreads.

The Group has, therefore, developed comprehensive funding and liquidity policies to ensure that it maintains sufficient liquid assets to be able to meet all its financial obligations and maintain public confidence.

Risk management (continued)

The Group's Treasury function is responsible for the day to day management of the Group's liquidity and wholesale funding. The Board sets limits over the level, composition, and maturity of liquidity and deposit funding balances, reviewing these at least annually. Compliance with these limits is monitored daily by Finance and Risk personnel independent of Treasury. Additionally, a series of liquidity stress tests are performed weekly by Risk and formally reported to the Asset and Liabilities Committee and the Board to ensure that the Group maintains adequate liquidity for business purposes even under stressed conditions.

The Group reports its liquidity position against its Liquidity Coverage Ratio, Net Stable Funding Ratio and other key regulatory ratios for regulatory purposes.

A liquid asset buffer of government Treasury Bills acquired under the FLS, and reserves with the Bank of England, are maintained as a source of high quality liquid assets that can be called upon to create sufficient liquidity in order to meet liabilities on demand.

Operational Risk

The Risk Committee received regular reports across the spectrum of operational risks and information security. These reports cover incidents that have arisen to allow the Committee to assess management's response and proposed remedial actions. Although a number of incidents were raised during the course of 2017, none of these was material in nature and the Committee was satisfied that the action taken was appropriate and that the control of operational incidents continued to improve. A test of the Group's Cyber Incident Response Plan was undertaken to assess the adequacy of the Group's internal control framework to respond to this threat and a maturity assessment of the Group's strategy to manage increasing levels of cyber risk in the market place was completed. The operational risk reports were developed throughout 2017 to include more focus on forward looking risks which permits a more strategic discussion at the Risk Committee level.

Conduct, Legal and Compliance Risk

The Group continually reviews its risk management approach to reflect the regulatory and legal environment in which the Bank operates.

The Group has no appetite for knowingly behaving inappropriately, resulting in unfair outcomes for its customers. During 2017 the Group appointed a Chief Compliance Officer to further develop its Risk Appetite for Conduct Risk and to introduce and embed measures across the conduct risk lifecycle, which includes product design, sales or after sales processes and culture. It also embedded revisions to annual product reviews and risk appetite to support the management of brokers, intermediaries and outsource partners. These measures are reported to the Board monthly and provide the basis for demonstrating that the Group is operating within its risk appetite. Where the Group identifies potential unintended outcomes for customers the Group uses its risk management process to proactively escalate, agreeing appropriate actions and communicating clearly with its customers to ensure a fair outcome is achieved. The Group also implemented three additional working groups to oversee complaints, Intermediaries and Brokers and Collections.

Strategic Risk

Strategic risk focusses on large, long term risks that could become a material issue for the delivery of the Group's goals and objectives. Management of strategic risk is primarily the responsibility of the Executive. The management of strategic risk is intrinsically linked to the corporate planning and stress testing processes and is further supported by the regular provision of consolidated business performance and risk reporting to the ExCo and the Board. The Board received and approved a number of reports during 2017 including the Strategy Update and the inception of the 2017 annual review of risk appetite. It has also been engaged actively in the formation of the Group's ICAAP and ILAAP which are critical tools to managing strategic risk.

Systems and Change Risk

Customer expectations for service availability are rising with the rapid pace of new technologies leading to a significantly lower tolerance for service disruption. The Group recognises that in order to continue to be recognised for very high levels of customer satisfaction it needs to continually monitor systems risk and ensure that change is delivered with minimum disruption to customers. During 2017 the Group reviewed its approach to managing change with a 'build the bank' and 'run the bank' focus across Change and Technology in line with its Target Operating Model.

Risk management (continued)

Top and emerging risks

The Group's top and emerging risks are identified through the process outlined in the 'Risk Management Framework' section and are considered regularly by management and subsequently by the Board Risk Committee. The Group sees seven themes as its top and emerging risks:

- Geopolitical Risk;
- Economic and Competitive Environment;
- Pace of Regulatory Change;
- Intermediary and Outsourcing;
- Pace, Scale of Change and Management Stretch;
- Credit Impairment; and
- Information Risk.

These themes, together with the Group's strategy to mitigate the risk and the direction of each theme, are considered further in the following sections:

Key: ↔ No Change ↓ Risk Decreased ↑ Risk Increased

Risk	Mitigation	Change
Geopolitical Risk **The Group's financial position continues to improve with increasing profitability and strong capital ratios. However, increasing Geopolitical risk presents a risk to the business, its financials and earnings volatility following an unprecedented political event.** **The UK has experienced a number of political events during 2017 including the UK government losing its majority in a snap election, increasing global populist trends, terrorist attacks and a weakening of Sterling. These risks have the potential to have an impact on the Group and the impact could be wide reaching affecting other risks such as economic, regulatory, business change, outsourcing, organisational and business change, regulation and conduct risk.**	The Group monitors the environment and its chosen markets on a regular basis and continues to prioritise RoTE over volume. The Group operates in specialist areas where management and staff have significant expertise and a deep understanding of customer needs to drive a long term relationship with its customers through the cycle. The Group undertakes a comprehensive assessment of its Risk Appetite and stress tests it's lending and deposit portfolios to ensure that it can meet its objectives in severe but plausible economic conditions. The Group regularly reviews its key outsource partners to establish Early Warning Indicators and to formalise exit plans.	↑ The UK economic outlook is expected to remain favourable in the short term but with increasing risks to the downside driven by weak productivity that may increase the potential for volatility for the Group and its customers. Developments regarding the UK's withdrawal from the EU – and in particular the reaction of households, businesses and asset prices to them – remain a significant influence on, and source of uncertainty about, the economic outlook.

Economic & Competitive Environment **A reversal in UK economic conditions, particularly in England where the majority of the Group's operations are based, could affect the Group's performance in a number of ways including:** • **lower demand for the Group's products and services;** • **changes in funding costs resulting from ongoing political uncertainty accompanied by a loss of confidence;** • **rising competition compressing Group margins below sustainable levels; and** • **higher impairments through increased defaults and/or reductions in collateral values.**	The Group uses its expertise and deep understanding of its customers' needs to drive customer service and long-term relationships with its customers through the cycle. The Group monitors its chosen markets on a regular basis and regularly reviews adjacent markets where it has expertise, and also reviews opportunities for inorganic growth.The Group operates in specialist areas where management and staff have significant expertise and a deep understanding of customer needs that delivers superior service. As a result, all loans are written thorough, bespoke underwriting to SMEs and consumers based on their ability to repay and, in the main, sufficient security. The Group undertakes a comprehensive assessment of its risk appetite to ensure that it can meet its objectives in severe but plausible economic conditions. The Group completes comprehensive stress testing of its lending and deposit portfolios to test resilience to severe but plausible economic conditions. The Group also establishes a prudent balance sheet strategy with robust levels of capital and liquidity and a prudent funding structure. The Group maintains risk appetite and pricing discipline.	↑ The UK economy remains resilient with near-term momentum and following 8-years of consecutive growth. However, the Board expects there to be a period of uncertainty with increased risks to the downside as Brexit negotiations continue.

Pace of Regulatory Change **The prudential and conduct regulatory regimes are subject to change and could lead to increases in the level and quality of capital that the Group needs to hold to meet regulatory requirements.** **The FPC in June 2017 announced the restoration of the countercyclical buffer (CCyB) to 0.5% with effect from June 2018. The FPC also confirmed on 28 November 2017 that the CCyB will increase from 0.5% to 1% with effect from November 2018 to lock in surplus capital in the PRA buffer to add resiliency to the market prior to Brexit.** **The Prudential Regulation Committee has indicated that it will set additional PRA buffers in light of the 2017 stress test results to reflect the judgement that, following recent rapid growth, the loss rate on consumer credit may be understated where they are based on benign recent conditions.** **The Financial Conduct Authority has undertaken a number of thematic reviews during 2017 including high cost consumer credit, a thematic review of consumer credit and has set out its plans for 2018.**	**The regulatory environment continues to evolve and change. The Group actively engages with regulators, industry bodies and advisors to actively engage in consultation processes.** **The Bank undertakes forward capital planning and sensitivity analysis using its ICAAP to ensure that the Bank has a long runway to respond to any changes in capital requirements.**	↑ **UK financial services businesses remain subject to significant scrutiny and the current level of risk is elevated when compared to last year.** **The Group adopts the Standardised Approach to its assessment of credit risk regulatory capital. The BCBS announced changes to the risk weightings under the Standardised Approach in December 2017 that will lead to an increase in capital requirements over the period of the strategic plan.** **The Group has completed its preparations to support adoption from 1 January 2018.** **The Group also remains on track to ensure it has a fully resourced plan to support GDPR compliance by 25 May 2018 including all necessary changes.** **The Bank completed an AT1 Issue of £125m in December 2017.**
Intermediary & Outsourcing **The Group is a specialist lending and savings bank for SMEs and consumers. The specialist nature of some of its lending through intermediaries and brokers could mean that some customers find themselves with an increased risk of an unfavourable outcome. For the Group this could also lead to increased conduct-related redress, additional fraud or credit risk impairments.**	The Group works with carefully selected intermediary and broker partners who take on the role of advising SMEs and consumers. The Group recognises that it is ultimately accountable for the lending it originates through its partners and continually undertakes reviews of their performance. The Group continually reviews its risk management approach to intermediaries, brokers and outsource partners to reflect the regulatory environment in which the Group operates.	↑ The Group continued to invest in its monitoring controls to manage its exposure to intermediaries, brokers and outsource partners during 2017 and believes that it continues to improve its risk profile. The Group's continued to invest in its relationship with Target Servicing Limited and is expected to further improve its outsourcing risk profile. The Group continues to explore other third party relationships through which to deliver its objectives.
Pace, Scale of Change and Management Stretch **The scale and pace of change could create delivery challenges and could lead to disruption of the Group's plans and in the delivery of its objectives.**	The Group understands the need to manage change without disrupting the Group's operating environment and impacting customer service. These operational risks are managed through a strong focus on change governance and programme management disciplines and are led by a dedicated Executive member. The risks are further mitigated by the Group's strengthening of the senior management team. The Group has a formal Operations Committee that is set-up to prioritise change and provide effective oversight of the change portfolio to ensure that requirements are delivered within budget and on time.	↔ The Group continues to invest in its change management processes to increase the pace and scale of change without impacting on the Group's operations and customer service. During 2017 this has focussed on the embedding of the new Target Operating Model and the implementation of the Chief Operating Office. However, the Group has a strong appetite for change and the risk of an impact on its operations remains.

Credit Impairment **At 31 December 2017 the Group had customer loans (including operating leases and net of impairment provisions) of £4.9 billion, and is exposed to credit impairment if customers are unable to repay loans and any outstanding interest and fees.** **In addition the Group has exposure to a small number of counterparties with whom it places surplus funding.**	The Group recognises that it will experience credit impairment in connection with its lending activities, but manages its exposure by: undertaking a prudent assessment of through-the-cycle losses in pricing, forecasting and stress testing; maintaining consistent and conservative loan-to-value ratios and avoiding material weakening of credit quality to drive volumes; lending predominantly on a secured basis against identifiable and accessible assets; operating strong controls and governance with effective oversight by a centralised Group credit team; and maintaining a prudent Treasury counterparty policy with surplus funding placed with the Bank of England and UK clearing banks.	↔ Underlying Group credit impairment has remained low, reflecting favourable market conditions in the UK and the Group's approach to lending. The Group's counterparty exposure has remained broadly unchanged with the majority of surplus funding placed with the Bank of England and balances with UK clearing banks. The Group believes that the potential for additional credit impairment has increased with uncertainty over the outlook of the Brexit negotiations and the outlook for the UK economy given recent forecasts of productivity and increasing consumer debt. The Group has completed its assessment of the impact of IFRS9 and will make use of the transition arrangements. The Group considers that its borrowers exposure to Carillion is minimal and has improved over 2017.
Information Risk **The pace of technological development is changing the way in which SMEs and consumers want to engage with the Group, leading to a number of risks:** • **increasing customer demand could exceed the Group's ability to provide highly reliable and widely available systems and services;** • **the evolving nature and scale of criminal activity could increase the likelihood and severity of attacks on the Group's systems; and** • **franchise value and customer trust could be significantly eroded by a sustained hack of the Group's systems leading to a diversion of funds or the theft of customer data.**	The Group continually reviews its control environment for information security to reflect the evolving nature of the threats to which the Group is exposed. The Group's strategy for mitigating information security risk is comprehensive, including: a documented cyber-strategy, ongoing threat assessments, regular penetration testing, the wide deployment of detective controls and a programme of education and training.	↑ The Group continues to invest in its capabilities to reduce its exposure to a cyber-attack and has further developed its risk appetite and controls with respect to information security. However, the risk of information security breaches, threats from cyber-crime and the impact of new technology on the Group's businesses remain.

ICAAP/ILAAP and Stress Testing

The ICAAP, ILAAP and associated stress testing exercises represent important elements of the Group's on-going risk management processes. The results of the risk assessment contained in these documents is embedded in the strategic planning process and risk appetite to ensure that sufficient capital and liquidity are available to support the Group's growth plans as well as cover its regulatory requirements at all times and under varying circumstances.

The ICAAP and ILAAP are reviewed at least annually, and more often in the event of a material change in capital or liquidity. On-going stress testing and scenario analysis outputs are used to inform the formal assessments and determination of required buffers, the strategy and planning for capital and liquidity management as well as the setting of Risk Appetite limits.

Risk management (continued)

The Board and Executive management have engaged in a number of exercises which have considered and developed stress test scenarios. The output analysis enables management to evaluate the Group's capital and funding resilience in the face of severe but plausible risk shocks. In addition to the UK variant test on capital prescribed by the Regulator, the stress tests have included a range of Group-wide, multi-risk category stress tests, generic and idiosyncratic financial shocks as well as operational risk scenario analyses. Stress testing is an integral part of the adequacy assessment processes for liquidity and capital, and the setting of tolerances under the annual review of Group Risk appetite.

The Group also performed reverse stress tests to help Executive management understand the full continuum of adverse impact and therefore the level of stress at which the Group would breach its individual capital and liquidity guidance requirements as set by the Regulator under the ICAAP and ILAAP processes.

Recovery Plan and Resolution Pack

The Group has prepared a Recovery Plan and Resolution Pack (RP&RP) in accordance with Prudential Regulatory Authority (PRA) Supervisory Statements SS18/13 and SS19/13. The Group is planning to update its RP&RP in 2018 to reflect the change in ownership.

The plan represents the Group's 'Living Will' and examines in detail:

- The consequences of severe levels of stress (i.e. beyond those in the ICAAP) impacting the Group at a future date;
- The state of preparedness and contingency plan to respond to and manage through such a set of circumstances; and
- The options available to Executive management to withstand and recover from such an environment.

This plan is prepared annually, or more frequently in the event of a material change in the Group's status, capital or liquidity position. The Board of Directors and senior management are fully engaged in considering the scenarios and options available for remedial actions to be undertaken.

The Board considers that the Group's business model, its supportive owners and the diversified nature of its business markets provides it with the flexibility to consider selective business or portfolio disposals, loan book run off, equity raising or a combination of these actions. The Group would invoke the Recovery Plan and a Resolution Pack in the event they are required.

Matters arising during the year:

During 2017, the Group has continued its strategy to embed the risk management framework (RMF) across the business, with a particular focus on first line defence and risk culture. The RMF has provided the Group with tools to ensure that minimum standards and requirements are met when identifying, assessing, monitoring and reporting risk. Throughout the year the Group Risk Committee ("the Committee") has monitored first line defence across the divisions further to ensure that the new RMF has been suitably embedded and that a culture of risk has been established. Across the year there have been events which have driven the Committee to undertake focussed reviews into responsible lending in the Property and Business Finance divisions, to ensure that that the risks are being managed adequately and that first and second line risk roles across the Group are defined appropriately.

Further to an FCA audit on the implementation of the Mortgage Conduct of Business Rules (MCOB) the Group has focused on ensuring that the procedures, policies and process in place for responsible lending are appropriate. This has included a review of affordability processes in all division with a particular focus on lending for second charge mortgages. The Risk Committee and the Audit Committee have jointly worked to ensure that training, procedures and policies adequately enhanced and align with FCA expectations.

The implementation of IFRS 9 has provided the Committee a chance to review the credit grading system which had recently been rolled out to all lending portfolios in the Group. This system will assist with the compliance with IFRS 9 and is providing enhanced credit management information, for reporting to the Committee and Board.

During 2017, an emerging risk arose around contingent liabilities , certain suppliers of goods and services to customers of the Group ' s Consumer Lending division, where such suppliers have gone into liquidation. The Committee has kept this under review across the year alongside the Audit Committee ensuring that the risks and responsibilities of the Group are being monitored and managed appropriately.

The Group undertook a Risk culture survey during the year, providing valuable feedback and comfort to the Committee surrounding on employees views and approach to risk. The survey was completed by 60% of participants and provided a good view of how risk is perceived across all divisions and central functions. Areas which have been highlighted for improvement will be further reviewed and monitored into 2018.

Risk management (continued)

Group viability statement

The Directors have assessed the outlook for the Group over a longer period than the twelve months required by the 'Going Concern' statement in accordance with the 2016 UK Corporate Governance Code.
The assessment relied on:

- The Board approved Strategic Update in December 2017 that outlines the business plans and financial projections from 31 December 2017 to 31 December 2021;
- The completion of an issuance of £125m of Additional Tier 1 in December 2017;
- The Internal Capital Adequacy Assessment Process ('ICAAP');
- The Internal Liquidity Adequacy Assessment Process ('ILAAP');
- A review and evaluation of its Top and Emerging Risks (as reported upon earlier in this section);
- Consideration of the effect of a moving regulatory landscape on the Pillar 2A, Pillar 2B and the CRD IV Combined Buffer requirements, together with the effect of the Group's Capital Contingency Plan to restore the capital position in scenarios of capital headwinds; and
- The effect of the implementation of the IFRS 9 'Financial Instruments', taking into account the phase-in arrangements published in the amended EU regulation No (EU) 575/2013.

The Group is not large enough to participate in the annual Bank of England concurrent stress testing programme but has, as part of its ICAAP, performed a variety of equivalent stress tests and reverse stress tests of its business. These include two market wide stress tests and five Group specific (idiosyncratic) stress tests. The stress tests were derived through discussions with Senior Management and the Board, after considering the Group's Top Risks. The Group also considered its funding and liquidity adequacy in the context of the reverse stress testing. The risk of the UK leaving the EU has been considered and the Board believe this risk was captured within its stress testing scenarios, and will keep this risk under review.

The stress tests enable the Group to assess the impact of a number of severe but plausible scenarios on its business model. In the case of reverse stress testing, the Board is able to assess scenarios and circumstances that would render its business model unviable, thereby identifying business vulnerabilities and ensuring the development of early warning indicators and potential mitigating actions.

The Board aims to build a sustainable lending and savings bank for SMEs and consumers over the medium to long term. The Board monitors a five-year Strategic Plan that provides a robust planning tool against which strategic decisions are made. Whilst the Board has no reason to believe that the Group will not be viable for a five-year period, given the inherent uncertainty involved, the Board concluded that a three year period is an appropriate length of time to perform a viability assessment with a greater level of certainty.

Based on the results of the above mentioned assessments, the Directors have a reasonable expectation that the Group will be able to continue in operation and meet its liabilities as they fall due over a period of at least three years.

Business review

The statutory results have been prepared in accordance with International Financial Reporting Standards (IFRS). Where appropriate, certain aspects of the results are presented to reflect the Board's view of the Group's underlying performance without distortions caused by non-recurring items that are not reflective of the Group's ongoing business activities.

Underlying results should be considered in addition to, and not as a substitute for, the Group's statutory results, and the Group's presentation of underlying results should not be construed as an indication that future results will be unaffected by exceptional items. Underlying results have limitations as analytical tools, and they should not be considered in isolation or as substitutes for analysis of the Group's results as reported on a statutory basis. Limitations may include, but are not limited to, the following:

- they may not reflect every cash expenditure, future requirements for capital expenditure or contractual commitments; and
- they may not reflect the impact of earnings or charges resulting from matters the Directors consider not to be indicative of ongoing operations.

Because of these limitations, underlying results are not intended as an alternative to the Group's statutory results or as an indicator of the Group's operating performance. The Group compensates for these limitations by using underlying results, along with other comparative tools, together with statutory results, to assist in the evaluation of operating performance.

The following items have been excluded from underlying results:
Costs of £0.2 million include expenses incurred during the year in relation to the offer from Marlin BidCo for the entire share capital of Shawbrook Group plc.

IFRS 2 charges amounting to £5.9 million were recognised in 2017 in respect of share-based awards made to employees that vested on Marlin BidCo gaining control of Shawbrook Group plc. IFRS 2 charges recognised in 2016 amounting to £2.2 million related to share-based awards to Steve Pateman, Chief executive Officer, which were fully satisfied by Special Opportunities Fund (Guernsey) LP. This was the result of a one-off award for compensation against forfeited long-term incentives at a previous employer.

Corporate activity costs of £0.4 million in 2017 relate to the cost of the incremental deposits raised to prefund the acquisition of a c.£190 million portfolio of property loans at the end of Q3 2017, which completed at the end of November 2017. In 2016 the costs of £10 million related to the cost of the incremental deposits raised to prefund the acquisition of the c.£300 million portfolio of property loans at the end of 2015, which completed in H2 2016. In both instances, during the period between acquisition and completion, the portfolio was funded by the vendor due to the length of the transition period, and reimbursed by Shawbrook, thus resulting in Shawbrook paying to fund the portfolio twice.

International Organization of Securities Commissions (IOSCO) regulation does not permit adjustment for items that are reasonably likely to occur in the foreseeable future, or activities that affected the entity's recent past, when considering underlying results as in their experience there are rarely circumstances where an explanation is sufficiently robust to result in restructuring costs or impairment losses being described as non-recurring. In addition, European Securities and Markets Authority (ESMA) regulation states that items which affected past periods and will affect future periods – such as restructuring costs or impairment losses – will rarely be considered as non-recurring, infrequent or unusual.

Business review (continued)

Profit and loss

	2017 (£m)	2016 (£m)
Interest income, net fee and operating lease income	**314.0**	292.7
Interest expense and similar charges	**(75.9)**	(83.0)
Net operating income	**238.1**	209.7
Costs and provisions for liabilities and charges	**(115.3)**	(96.3)
Impairment losses on financial assets	**(23.3)**	(24.3)
Statutory profit before taxation	**99.5**	89.1

Underlying adjustments		
Project Marlin costs	**0.2**	-
IFRS 2 charge	**5.9**	2.2
Corporate activity costs	**0.4**	1.0
Underlying profit before taxation	**106.0**	92.3

Performance

The Group's underlying profit before tax has improved from £92.3m in 2016 to £106.0m in 2017 due to the growth in the Group's asset base, lower cost of funds and the benefits that increased efficiencies of scale in the Group's infrastructure create. This improvement is against the background of a competitive market where margins have seen some compression in some of the Group's divisions.

Key performance indicators

	2017		**2016**	
Year ended 31 December	**Statutory**	**Underlying**	**Statutory**	**Underlying**
Profit before tax (£m)	99.5	106.0	89.1	92.3
Loans and advances to customers (£m)(1)	4,880.4	4,880.4	4,088.5	4,088.5
Average principal employed (£m)	4,424.9	4,424.9	3,769.3	3,769.3
Net interest margin (%)(2)	5.4	5.4	5.6	5.6
Return on tangible equity (%)(3)	18.4	19.9	19.2	19.9
CET1 ratio (%)(4)	12.8	12.8	13.2	13.2
Total capital ratio (%)(5)	19.1	19.1	16.3	16.3
Leverage ratio (%)(6)	9.4	9.4	7.7	7.7
Cost to income ratio (%)	48.4	45.7	45.9	44.7

1) Net loans include loans and advances to customers net of impairment provision plus operating leases.
2) Net interest margin is calculated as underlying net operating income divided by average principal employed.
3) Return on tangible equity is calculated as profit for the year attributable to owners divided by average tangible equity. Average tangible equity is calculated as total equity less intangible assets at the beginning of a period plus total equity less intangible assets at the end of the period, divided by two.
4) *CET1 ratio is calculated as the total core equity capital divided by the risk-weighted assets.*
5) Total capital ratio is calculated as total capital for regulatory purposes divided by risk-weighted assets.
6) Leverage ratio is calculated as tier 1 capital divided by total assets.

Business review (continued)

Underlying PBT in 2017 increased to £106.0m (2016: £92.3m) and statutory profit increased to £99.5m (2016: £89.1m). This increased profitability has been driven by an increase in the loan book (including operating leases) to £4,880.4m (2016: £4,088.5m).

Net interest margin remained stable at 5.4% (2016: 5.6%) and underlying return on tangible equity remained at 19.9% in 2017 (2016: 19.9%).

Capital decreased marginally resulting in a CET1 ratio of 12.8% (2016: 13.2%). Total capital ratio increased from 16.3% in 2016 to 19.1% in 2017 while the leverage ratio increased from 7.7% in 2016 to 9.4% in 2017.

Cost to income ratio increased from 44.7% in 2016 to 45.7% in 2017 due to growth in income coupled with continued operational efficiencies across the three divisions and the central functions.

Divisional performance

The Group has four reportable operating segments as described below which are based on the Group's three lending divisions plus a Central segment which represents the Retail Savings business, central functions and shared central costs. Operating segments are reported in a manner consistent with the internal reporting provided to the Chief Executive Officer, who is considered to be the Chief Decision Making Officer.

Year ended 31 December 2017	**Property Finance £m**	**Business Finance £m**	**Consumer Lending £m**	**Central £m**	**Total £m**
Net interest, fee and operating lease income	**175.6**	**88.7**	**44.5**	**5.2**	**314.0**
Interest expense and similar charges	**(41.1)**	**(13.2)**	**(8.2)**	**(13.4)**	**(75.9)**
Net operating income	**134.5**	**75.5**	**36.3**	**(8.2)**	**238.1**
Costs and provisions	**(17.1)**	**(16.7)**	**(15.5)**	**(66.0)**	**(115.3)**
Impairment losses on financial assets	**(2.4)**	**(8.5)**	**(12.4)**	**-**	**(23.3)**
Profit/(loss) before tax	**115.0**	**50.3**	**8.4**	**(74.2)**	**99.5**

Year ended 31 December 2016	Property Finance £m	Business Finance £m	Consumer Lending £m	Central £m	Total £m
Net interest, fee and operating lease income	152.6	91.5	43.0	5.6	292.7
Interest expense and similar charges	(52.8)	(21.2)	(9.9)	0.9	(83.0)
Net operating income	99.8	70.3	33.1	6.5	209.7
Costs and provisions	(15.2)	(16.3)	(10.8)	(54.0)	(96.3)
Impairment losses on financial assets	(2.1)	(14.5)	(7.7)	-	(24.3)
Profit/(loss) before tax	82.5	39.5	14.6	(47.5)	89.1

The Strategic report was approved by the Board of Directors on 7 March 2018 and was signed on its behalf by:

Steve Pateman
Chief Executive Officer

Statement of Directors' responsibilities in respect of the Annual Report and Accounts

The directors are responsible for preparing the Annual Report and the Group and parent Company financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare Group and parent Company financial statements for each financial year. Under that law they have elected to prepare the Group and parent Company financial statements in accordance with International Financial Reporting Standards as adopted by the EU (IFRSs as adopted by the EU) and applicable law.

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Group and parent Company and of their profit or loss for that period. In preparing each of the Group and parent Company financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, relevant and reliable;
- state whether they have been prepared in accordance with IFRSs as adopted by the EU;
- assess the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and
- use the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the parent Company's transactions and disclose with reasonable accuracy at any time the financial position of the parent Company and enable them to ensure that its financial statements comply with the Companies Act 2006. They are responsible for such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error, and have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Group and to prevent and detect fraud and other irregularities.

Daniel Rushbrook
Company Secretary
7 March 2018

Directors' report

The Directors present their Annual Report and Accounts for the year ended 31 December 2017.

Principal activities

The Company and its subsidiaries comprise the 'Group'. The Company is a banking institution which is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority.
Its principal activities are:

- Taking of retail deposits;
- Provision of secured and unsecured consumer loans;
- Provision of secured commercial loans;
- Provision of asset finance;
- Provision of wholesale finance; and
- Provision of invoice discounting.

Results for the year

The Group made a profit before tax for the year of £99.5m (2016: £89.1m) and a profit after tax of £74.2m (2016: £65.7m).

The Company made a profit before tax for the year of £100.2m (2016: £89.1m) and a profit after tax of £74.9m (2016: £65.7m).

Board composition

The Directors who served during the year were:
Robin Ashton
Iain Cornish
Cédric Dubourdieu (appointed on 5 September 2017)
Sally-Ann Hibberd
Paul Lawrence
Roger Lovering
Stephen Johnson (resigned on 23 January 2018)
Lindsey McMurray
David Gagie
Steve Pateman
Andrew Didham (appointed on 1 February 2017)
Dylan Minto (appointed on 6 February 2017)

The Company Secretary for the year was Daniel Rushbrook.

Dividends

The Directors do not recommend the payment of a dividend for the ended 31 December 2017.

Share capital

Shawbrook Bank Limited is a company limited by shares.

Details of the Bank's issued share capital, are shown on page 70 in Note 26.

Employees

The Group is committed to being an equal opportunities employer and opposes all forms of discrimination. Applications from people with disabilities will be considered fairly and if existing employees become disabled, every effort is made to retain them within the workforce wherever reasonable and practicable. The Group also endeavours to provide equal opportunities in the training, promotion and general career development of disabled employees.
The Group regularly provides employees with information of concern to them, which incorporates the Group's current performance and its future aims and strategies. The Group conducts an Annual Employee Survey and uses the results of this survey to improve performance in areas that are important to staff. A monthly newsletter providing business updates and background information on the Group is circulated to all staff.

Directors' Interest in the shares of the Company

The Directors of the Group have no interest in the share capital of the Company. The Company is a wholly owned subsidiary of Shawbrook Group plc.

Rights of the shareholders of the Company

Holders of the shares of the Company are entitled to dividends as decided from time to time and are entitled to one vote per share at general meetings of the Company. There are no restrictions on the rights implicit to these shares.

Directors' Report (Continued)

Information presented in other sections of this document
The Directors elected to present the following information in other sections of this document. The likely future developments are discussed in the Group viability statement on page 18 of the Strategic report. Information on financial instruments, financial risk management objectives and policies are described on pages 72 to 94 of the Financial Statements.

Research and development activities
During the ordinary course of business the Bank develops new products and services within the business units.

Branches
The Bank operates in the United Kingdom and has a branch in Jersey.

Post balance sheet events
On 23 February 2018, the Group received confirmation of an interim payment of £4.95 million relating to the Group's insurance claim in respect of the controls breach identified in the Business Finance Division in H1 2016, which will be paid subject to verification of the quantum of the claimed losses. The Group's insurers confirmed that the Group's insurance claim is covered in principle under the policy, but insurers are still considering certain aspects of the Group's claim before the final settlement amount can be determined.
There have been no other significant events between 31 December 2017 and the date of approval of the financial statements which would require a change to or additional disclosure in the financial statements.

Political and charitable contributions
The Group made charitable donations of £42k during the year (2016: £102k).The Group did not make any political donations during the year (2016: £nil).

Slavery and human trafficking
In the financial year ended 31 December 2017, the Group took the following steps to ensure slavery and human trafficking did not occur within the organisation or supply chain:

- identifying and addressing risks: the Group has updated its processes for evaluating prospective suppliers and reviewing existing suppliers to understand its suppliers' self-assessment of slavery and human trafficking issues;
- developing policy: the Group has and continues to update its compliance policies to include consideration of slavery and human trafficking issues (as applicable); and
- training: the Group has made available training to those of its staff who deal most with its suppliers. Development of an intranet resources page is also underway which staff will be able to access to learn about modem slavery and human trafficking.

Directors' and officers' insurance
The Group has maintained appropriate Directors' and Officers' liability insurance in place throughout 2017.

Going concern
The financial statements are prepared on a going concem basis, as the Directors are satisfied that the Group has the resources to continue in business for the twelve months from the reporting date. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the balance sheet, future projections of profitability, cash flows and capital resources and the longer term strategy of the business. The Group's capital and liquidity plans, including stress tests, have been reviewed by the Directors.

The Group's forecasts and projections show that it will be able to operate at adequate levels of both liquidity and capital for the twelve months from the reporting date, including a range of stressed scenarios, the availability of alternative sources of capital if required and appropriate management actions.

After making due enquiries, the Directors believe that the Group has sufficient resources to continue its activities for the twelve months from the reporting date and to continue its expansion, and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the Prudential Regulation Authority.

Disclosure of information to the auditor

The Directors confirm that:

1. so far as each of the Directors is aware, there is no relevant audit information of which the auditor is unaware; and
2. the Directors have taken all the steps that they ought to have taken as Directors in order to make themselves aware of any relevant audit information and to establish that the auditor is aware of that information.
   This confirmation is given and should be interpreted in accordance with the provisions of the Companies Act 2006.

Auditor

Resolutions to reappoint KPMG LLP as the Group's auditor and to give the directors the authority to determine the auditor's remuneration will be proposed at the annual general meeting.

By order of the Board

Steve Pateman
Chief Executive Officer
7 March 2018

KPMG

Independent auditor's report

to the members of Shawbrook Bank Limited

1. **Our opinion is unmodified**

We have audited the financial statements of Shawbrook Bank Limited ("the Company") for the year ended 31 December 2017 which comprise the Consolidated Statement of Profit and Loss and Other Comprehensive Income, Consolidated and Company Statements of Financial Position, Consolidated Statement of Equity, Company Statement of Equity and Consolidated and Company Statements of Cash Flows, and the related notes, including the accounting policies.

In our opinion:

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

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the audit committee.

We were appointed as auditor by the directors in June 2011. The period of total uninterrupted engagement is for the 7 financial years ended 31 December 2017. We have fulfilled our ethical responsibilities under, and we remain independent of the Group in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to public interest entities. No non-audit services prohibited by that standard were provided.

Overview		
Materiality: group financial statements as a whole	£5.1m (2016:£4.2m) 4.8% (2016: 4.8%) of normalised profit before tax (2016: profit before tax)	
Coverage	100% (2016:100%) of group profit before tax	
Risks of material misstatement		**vs 2016**
Recurring risks	Impairment provisioning	◄►
	Effective interest rate accounting	◄►
	Valuation of goodwill	◄►
Event driven	**New:** Provisions for conduct related matters	▲

2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team.

Our assessment of the Group's, and the Company's, significant risks was the starting point for our audit. This considered both internal and external risks to the Group's business model and how these have been mitigated.

The internal factors considered were:

Control environment – we considered the Group's control environment and in particular whether its systems were processing transactions completely and faithfully, and included appropriate controls designed to prevent fraud;

Capital and liquidity – we considered the strength of the Group's capital and liquidity position, the diversification of assets, the flexibility and composition of its balance sheet and the management of its cost base; and

Business activity – we assessed the risk in relation to new and one-off transactions including newly acquired loan portfolios and the Group's delisting, as well as the impact of portfolio seasoning on loan impairment and redemption behaviour.

The external factors considered were:

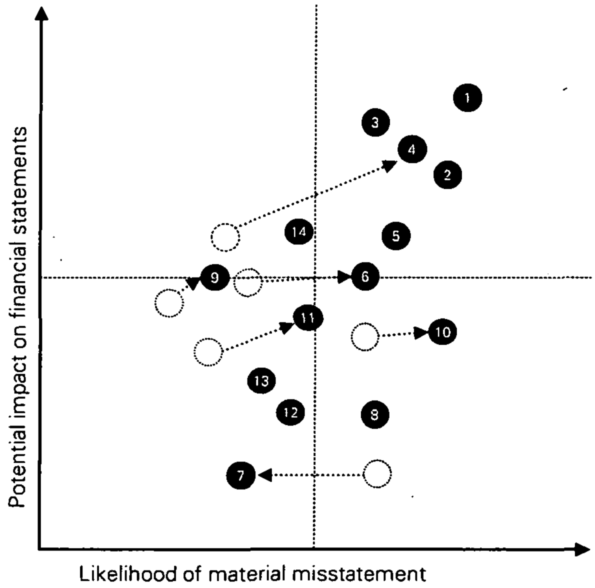
Economic changes - we consider the audit risk in relation to loan impairment and goodwill to have been affected by the impact on the economy of the result of the EU referendum, which introduces unpredictability of forecasting in comparison to the previously benign market.

Political and regulatory changes – the regulatory and tax changes in the buy-to-let market, together with greater competition in this market, have introduced increased uncertainty over the expected remaining lives of current buy-to-let lending.

Market developments – increasing levels of competition in the market, and the advancement of technological solutions, including the upcoming changes from Open Banking.

Our assessment of key risks continued from our initial planning throughout our interim and final audits and was regularly updated through ongoing conversations with management, the Board and Audit Committee. This consideration includes conversations not only with the Group, and ongoing knowledge gained through reading pertinent information, but also reflected the views of the Prudential Regulatory Authority, market analysts, specialists within our firm, and peer comparisons.

Consistent with 2016, we are of the view that loan impairment, recognition of revenue in relation to effective interest rate accounting and the valuation of goodwill carry the greatest significance. One new key audit matter has been included this year in relation to conduct related provisions.



- Significant financial statement audit risks
- Other areas of audit focus
- Significant risk as mandated by International Standards on Auditing

1. Impairment provisioning
2. Effective interest rate accounting
3. Valuation of goodwill
4. Conduct risk
5. Management override of controls
6. Hedge accounting
7. Share option schemes
8. Cost capitalisation
9. Taxation
10. Financial statement disclosure
11. Valuation of financial instruments – derivatives
12. Valuation of financial instruments – amortised cost and level 3 fair value
13. Residual value risk
14. Loan portfolio acquisition accounting

We summarise on the following pages the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed, and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

	The risk	Our response
Impairment provisioning (£31.6 million; 2016: £24.4 million) *Refer to note 13 of the financial statements.*	**Subjective estimate** The calculation of certain impairment provisions for the Group is inherently judgemental. Individual and collective impairment provisions (identified and unidentified) may not reflect recent developments in credit quality, arrears experience, or emerging macro-economic risks. The most significant areas are: *Individual provisions* For the modelled individual provisions (consumer finance and second charge mortgages) the key judgements are the probabilities of default (PDs). These judgements are particularly subjective because the Group has limited historical experience to support the assumptions made due to the relatively unseasoned nature of its loan portfolios underwritten during a relatively benign economic period. Business Finance and Commercial loans are monitored and placed on a watch list if they are considered to exhibit evidence of impairment. Provisioning judgements are then made for these loans based on the individual circumstances of each case and expectations of future cash flows. These individually assessed provisions are particularly judgemental for these portfolios where the nature of collateral and exit strategy selected can significantly impact the timing and value of cash flows. *Collective provisions* The key judgements in the collective provisioning model are the emergence period, probability of default and loss given default. The emergence period is the most difficult judgement to estimate due to the difficulty of obtaining historical data. Alongside the above, another area of focus is post modelling adjustments and management overlays as they have the potential to be significant, judgemental and may be difficult to corroborate.	Each of our procedures were applicable to the Company and the Group. Our procedures included: — **Control testing:** We tested the design, implementation and operating effectiveness of key controls over the monitoring and reporting of loans and advances to customers; — **Sensitivity analysis:** We assessed and challenged the reasonableness of the Group's key assumptions, being the propensity to default, loss given default and emergence periods, performing stress tests; — **Assessing transparency:** Considering the adequacy of the Group's disclosures in respect of the sensitivity of impairment provisions to these assumptions. For loans assessed for individual provisions: — **Our credit experience:** We examined a risk based sample of business finance and commercial mortgage exposures including impaired and unimpaired loans and formed our own judgement, based on the individual facts and circumstances, as to whether impairment was required. This included an assessment of the supporting evidence for collateral valuations. — **Independent re-performance:** We re-performed a sample of calculations of impairment and agreed the key data inputs to source documentation; and — **Our sector experience:** We challenged and assessed the reasonableness of the key judgemental areas of the calculation, being forecast sale value of the collateral through benchmarking and back-testing to historical experience. For loans assessed collectively for impairment: — **Our sector experience:** We critically assessed the assumptions inherent in the model against our understanding of the different loan portfolios across the Group, their recent performance and industry developments; and — **Management overlay:** We critically assessed the rationale for quantum of overlay maintained with reference to our own knowledge of the industry and findings from our audit of the models. **Our results** — We found the resulting estimate for impairment provisioning to be acceptable.

	The risk	Our response
Valuation of goodwill (£38.5 million; 2016: £38.5 million) *Refer note 16 of the financial statements.*	**Forecast-based valuation** The carrying value of goodwill is tested for impairment on the occurrence of an impairment trigger or otherwise annually. The estimated recoverable amount is subjective due to the inherent uncertainty involved in forecasting future cash flows and selecting an appropriate discount rate. £34.7 million of the total goodwill balance relates to Business Finance, being the area of most significant judgement in light of the size of the balance and weaker than expected financial performance in the year.	Our procedures included: — **Our sector experience:** Evaluating assumptions used, in particular those relating to forecast revenue growth, discount rate and incremental capital requirements in Business Finance; — **Benchmarking assumptions:** Comparing the Group's assumptions to external comparable data in relation to key inputs such as projected economic growth and discount rates; — **Sensitivity analysis:** Performing breakeven analysis on the assumptions noted above using our data analytic capabilities; and — **Assessing transparency:** Assessing whether the Group's disclosures about the sensitivity of the outcome of the impairment assessment to changes in key assumptions reflected the risks inherent in the valuation of goodwill. **Our results** — We found the resulting estimate of the carrying value of goodwill to be acceptable.
Provisions for conduct related matters (£2.5 million; 2016: £nil) *Refer to notes 22 and 34 of the financial statements.*	**Estimation of exposure** Certain of the Group's lending activities give rise to ongoing exposure under Section 75 Consumer Credit Act. During the year, the Group saw an increase in customer complaints relating to its solar lending product where the original supplier is no longer solvent. The application of accounting standards to determine the amount, if any, to be provided as a liability and the associated disclosure, is inherently subjective.	Each of our procedures were applicable to the Company and the Group. Our procedures included: — **Enquiry of management:** We enquired of the Directors and key members of legal, risk and compliance to obtain their view on the status of all significant litigation and regulatory matters and the completeness of their assessment in respect of these provisions; — **Independent evaluation:** inspecting internal papers and regulatory correspondence we challenged the timing of the recognition of provisions where there is potential exposure but it is not clear whether an obligation exists or where the Group have determined a reliable estimate is not possible. We independently evaluated the provision estimated including a re-performance of management's calculations; and — **Assessing transparency:** Assessing whether the group's disclosures detailing significant conduct related matters adequately disclose the potential liabilities of the Group. **Our results** — We found the liability recognised, and the associated disclosure, to be acceptable.

	The risk	Our response
Effective interest rate accounting ('EIR') Interest paid by customers £307.1 million (2016: £279.0 million); *Refer to note 2 of the financial statements.*	**Subjective estimate** Interest and fees, including early redemption charges, earned on loans are recognised using the effective interest rate method which spreads directly attributable cash flows over the expected lives of the loans. The Group apply judgement in deciding which cash flows are spread on an EIR basis and assessing the redemption profiles used to spread those cash flows. The most critical element of judgement in this area is the estimation of the redemption profiles of the loans, informed by past customer behaviour of when loans have been paid off.	Each of our procedures were applicable to the Company and the Group. Our procedures included: — **Methodology choice:** We tested the accuracy of data inputs from the mortgage systems into the effective interest rate models and the consistency of methodology and application across the Group's loan portfolios; — **Independent re-performance:** We evaluated the mathematical accuracy of models through re-performance of the model calculations; — **Sensitivity analysis:** We assessed and challenged the reasonableness of the models' key assumptions, expected lives and forecast future cash flows, by comparing these to historical trends within the Group and performing stress tests; and — **Assessing transparency:** Considering the adequacy of the Group's disclosures in respect of the sensitivity of the revenue to these assumptions. **Our results** — We found the amount of interest paid by customers recognised in the year to be acceptable.

3. Our application of materiality and an overview of the scope of our audit

Materiality

Materiality for the group financial statements as a whole was set at £5.1m (2016: £4.2m), determined with reference to a benchmark of group profit before tax, normalised to exclude this year's accelerated IFRS2 charge in relation to the acquisition of the Bank's parent company as disclosed in note 9 and totalling £5.9m (of which it represents 4.8% (2016: 4.8%).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £0.3m, in addition to other identified misstatements that warranted reporting on qualitative grounds.

Materiality for the parent company financial statements as a whole was set at £5.1m (2016: £4.2m) consistent with that of the Group as the parent company represents 100% of the Group's profit.

Team structure

The Group team performed the audit of the Group as if it was a single aggregated set of financial information. The audit was performed using the materiality level set out above.

Scope – disclosure of IFRS 9 effect

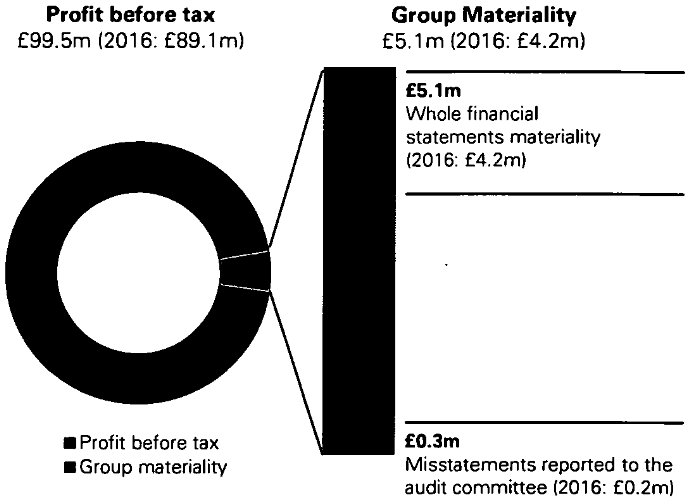
The Group is adopting IFRS 9 Financial Instruments from 1 January 2018 and has included an estimate of the financial impact of the change in accounting standard in accordance with IAS 8 Changes in Accounting Estimates and Errors as set out in note 1.10. This disclosure notes that the estimate has been prepared under an interim control environment with models that continue to undergo validation. While further testing of the financial impact will be performed as part of our 2018 year end audit, we have performed sufficient audit procedures for the purposes of assessing the disclosures made in accordance with IAS 8. Specifically we have:

— considered key classification and measurement decisions, including business model assessments and solely payment of principal and interest outcomes;

— considered the appropriateness of key technical decisions, judgements, assumptions and elections made in determining the estimate;

— involved credit risk modelling and economic specialists in the consideration of credit risk modelling decisions and macroeconomic variables, including forward economic guidance and generation of multiple economic scenarios, for a sample of models used in determining the estimate;

— considered interim controls and governance processes related to the calculation and approval of the estimated transitional impact.



4. We have nothing to report on going concern

We are required to report to you if we have concluded that the use of the going concern basis of accounting is inappropriate or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

5. We have nothing to report on the strategic report and the directors' report

The directors are responsible for the strategic report and the directors' report. Our opinion on the financial statements does not cover those reports and we do not express an audit opinion thereon.

Our responsibility is to read the strategic report and the directors' report and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work:

— we have not identified material misstatements in those reports;

— in our opinion the information given in the strategic report and the directors' report for the financial year is consistent with the financial statements; and

— in our opinion those reports have been prepared in accordance with the Companies Act 2006.

6. We have nothing to report on the other matters on which we are required to report by exception

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

— adequate accounting records have not been kept by the parent Company, or returns adequate for our audit have not been received from branches not visited by us; or

— the parent Company financial statements are not in agreement with the accounting records and returns; or

— certain disclosures of directors' remuneration specified by law are not made; or

— we have not received all the information and explanations we require for our audit.

We have nothing to report in these respects.

7. Respective responsibilities

Directors' responsibilities

As explained more fully in their statement set out on page 22 ~~XX~~, the Directors are responsible for: the preparation of the financial statements including being satisfied that they give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Group and parent Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Group or the parent Company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities

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

A fuller description of our responsibilities is provided on the FRC's website at www.frc.org.uk/auditorsresponsibilities.

Irregularities – ability to detect

We identified areas of laws and regulations that could reasonably be expected to have a material effect on the financial statements from our sector experience, through discussion with the directors and other management (as required by auditing standards), and from inspection of the group's regulatory and legal correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related company legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related annual accounts items.

In addition we considered the impact of laws and regulations in the specific areas of regulatory capital and liquidity, conduct, money laundering, and financial crime and certain aspects of company legislation recognising the regulated nature of the group's activities. With the exception of any known or possible non-compliance, and as required by auditing standards, our work in respect of these was limited to enquiry of the directors and other management and inspection of regulatory and legal correspondence. We considered the effect of any known or possible non-compliance in these areas as part of our procedures on the related annual accounts items. Further detail in respect of conduct related matters is set out in the key audit matter disclosures in section 2 of this report.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

As with any audit, there remained a higher risk of non-detection of non-compliance with relevant laws and regulations (irregularities), as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls.

8. The purpose of our audit work and to whom we owe our responsibilities

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

Simon Ryder (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
15 Canada Square
London
E14 5GL
7 March 2018

Consolidated statement of profit and loss and other comprehensive income

For the year ended 31 December 2017

	Notes	2017 £m	Restated[1] 2016 £m
Interest and similar income	2	**313.3**	284.4
Interest expense and similar charges	3	**(75.9)**	(83.0)
Net interest income		**237.4**	201.4
Operating lease rentals		**12.3**	13.5
Other income		**-**	0.1
Depreciation on operating leases	15	**(10.6)**	(11.3)
Net income from operating leases		**1.7**	2.3
Fee and commission income	4	**12.3**	11.2
Fee and commission expense		**(13.5)**	(5.7)
Net fee and commission (expense)/income		**(1.2)**	5.5
Fair value gains on financial instruments	14	**0.2**	0.5
Net operating income		**238.1**	209.7
Administrative expenses	5	**(113.2)**	(95.2)
Impairment losses on loans and advances to customers	13	**(23.3)**	(24.3)
Provisions for liabilities and charges	22	**(2.1)**	(1.1)
Total operating expenses		**(138.6)**	(120.6)
Profit before taxation		**99.5**	89.1
Income tax charge	11	**(25.3)**	(23.4)
Profit after taxation, being total comprehensive income, attributable to owners		**74.2**	65.7

The notes on pages 38 to 98 are an integral part of these financial statements.

[1] Refer to Note 1.8 for details of the restatement.

Consolidated and Company statement of financial position

As at 31 December 2017

	Notes	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Assets					
Cash and balances at central banks		**752.5**	**752.5**	429.9	429.9
Loans and advances to banks		**28.8**	**28.5**	24.1	24.1
Loans and advances to customers	12	**4,844.3**	**4,799.3**	4,050.4	4,050.4
Derivative financial assets	14	**1.8**	**1.8**	5.2	5.2
Property, plant and equipment	15	**39.6**	**39.2**	42.6	42.6
Intangible assets	16	**59.4**	**44.6**	53.6	38.8
Deferred tax assets	17	**15.7**	**15.7**	17.9	17.9
Other assets	18	**9.9**	**19.8**	16.1	16.1
Total assets		**5,752.0**	**5,701.4**	4,639.8	4,625.0
Liabilities					
Customer deposits	20	**4,376.2**	**4,376.2**	3,943.5	3,943.5
Amounts due to banks	21	**607.3**	**607.3**	147.7	147.7
Provisions for liabilities and charges	22	**2.8**	**2.8**	1.3	1.3
Derivative financial liabilities	14	**3.4**	**3.4**	0.4	0.4
Current tax liabilities		**7.8**	**7.8**	14.2	14.2
Other liabilities	23	**63.4**	**26.8**	28.8	28.7
Subordinated debt liability	25	**76.1**	**76.1**	76.1	76.1
Total liabilities		**5,137.0**	**5,100.4**	4,212.0	4,211.9
Equity					
Share capital	26	**175.5**	**175.5**	175.5	175.5
Capital securities	27	**125.0**	**125.0**	-	-
Share premium account		**81.0**	**81.0**	81.0	81.0
Merger reserve		**1.6**	**1.6**	1.6	1.6
Capital redemption reserve		**16.7**	**16.7**	9.2	9.2
Retained earnings		**215.2**	**201.2**	160.5	145.8
Total equity		**615.0**	**601.0**	427.8	413.1
Total equity and liabilities		**5,752.0**	**5,701.4**	4,639.8	4,625.0

The notes on pages 38 to 98 are an integral part of these financial statements.

These financial statements were approved by the Board of Directors on 7 March 2018 and were signed on its behalf by:

Steve Pateman
Chief Executive Officer

Dylan Minto
Chief Financial Officer

Registered number 07240248

Consolidated statement of changes in equity

For the year ended 31 December 2017

	Share capital £m	Capital securities £m	Share premium account £m	Merger reserve £m	Capital redemption reserve £m	Retained earnings £m	Total equity £m
Balance as at 1 January 2016	175.5	-	81.0	1.6	4.4	94.8	357.3
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	65.7	65.7
Total comprehensive income for the year	-	-	-	-	-	65.7	65.7
Share-based payments	-	-	-	-	4.8	-	4.8
Balance as at 31 December 2016	175.5	-	81.0	1.6	9.2	160.5	427.8
Balance as at 1 January 2017	175.5	-	81.0	1.6	9.2	160.5	427.8
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	**74.2**	**74.2**
Total comprehensive income for the year	-	-	-	-	-	**74.2**	**74.2**
Transactions with owners recorded directly in equity							
Dividend paid	-	-	-	-	-	**(19.5)**	**(19.5)**
Total contributions by and distributions to owners	-	-	-	-	-	**(19.5)**	**(19.5)**
Transactions with non-controlling entities							
Issue of capital securities	-	**125.0**	-	-	-	-	**125.0**
Total contributions by non-controlling entities	-	**125.0**	-	-	-	-	**125.0**
Share-based payments	-	-	-	-	**7.5**	-	**7.5**
Balance as at 31 December 2017	**175.5**	**125.0**	**81.0**	**1.6**	**16.7**	**215.2**	**615.0**

The notes on pages 38 to 98 are an integral part of these financial statements.

Company statement of changes in equity

For the year ended 31 December 2017

	Share capital £m	Capital securities £m	Share premium account £m	Merger reserve £m	Capital redemption reserve £m	Retained earnings £m	Total equity £m
Balance as at 1 January 2016	175.5	-	81.0	1.6	4.4	79.7	342.2
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	66.1	66.1
Total comprehensive income for the year	-	-	-	-	-	66.1	66.1
Share-based payments	-	-	-		4.8	-	4.8
Balance as at 31 December 2016	175.5	-	81.0	1.6	9.2	145.8	413.1
Balance as at 1 January 2017	175.5	-	81.0	1.6	9.2	145.8	413.1
Total comprehensive income for the year							
Profit for the year	-	-	-	-	-	**74.9**	**74.9**
Total comprehensive income for the year	-	-	-	-	-	**74.9**	**74.9**
Transactions with owners recorded directly in equity							
Dividend paid	-	-	-	-	-	**(19.5)**	**(19.5)**
Total contributions by and distributions to owners	-	-	-	-	-	**(19.5)**	**(19.5)**
Transactions with non-controlling entities							
Issue of capital securities	-	**125.0**	-	-	-	-	**125.0**
Total contributions by non-controlling entities	-	**125.0**	-	-	-	-	**125.0**
Share-based payments	-	-	-	-	**7.5**	-	**7.5**
Balance as at 31 December 2017	**175.5**	**125.0**	**81.0**	**1.6**	**16.7**	**201.2**	**601.0**

The notes on pages 38 to 98 are an integral part of these financial statements.

Consolidated and Company statement of cash flows

For the year ended 31 December 2017

	Notes	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Cash flows from operating activities					
Profit/(loss) for the year before taxation		99.5	100.2	89.1	89.5
Adjustments for non-cash items	28	54.4	54.3	51.7	51.3
Cash flows from operating activities before changes in operating assets and liabilities		**153.9**	**154.5**	140.8	140.8
Increase/decrease in operating assets and liabilities					
Increase in mandatory balances with central banks		(0.3)	(0.3)	(1.7)	(1.7)
Increase in loans and advances to customers		(817.2)	(772.1)	(755.6)	(755.6)
Increase in operating lease assets		(8.6)	(8.2)	(7.5)	(7.5)
Decrease/(increase) in derivatives		6.4	6.4	(2.0)	(2.0)
Decrease/(increase) in other assets		6.2	(3.7)	(8.7)	(8.7)
Increase in subordinated debt receivable		-	-	-	
Increase in customer deposits		432.7	432.7	757.1	757.1
Increase in provisions for liabilities and charges		1.5	1.5	0.4	0.4
Increase/(decrease) in other liabilities		34.6	(1.9)	(297.4)	(297.4)
Net change in operating assets and liabilities		**(344.7)**	**(345.6)**	(315.4)	(315.4)
Tax (paid)/received		(29.5)	(29.5)	(20.5)	(20.5)
Net cash flow (used by)/generated from operating activities		**(220.3)**	**(220.6)**	(195.1)	(195.1)
Cash flows from investing activities					
Purchase of property, plant and equipment	15	(1.6)	(1.6)	(0.2)	(0.2)
Sale of property, plant and equipment		-	-	0.2	0.2
Purchase of intangible assets	16	(9.8)	(9.8)	(7.9)	(7.9)
Net cash used by investing activities		**(11.4)**	**(11.4)**	(7.9)	(7.9)
Cash flows from financing activities					
Increase in amounts due to banks		459.6	459.6	107.8	107.8
Payment of subordinated debt interest		(6.4)	(6.4)	(5.3)	(5.3)
Net proceeds from the issue of capital securities		125.0	125.0	-	-
Dividends paid to Shareholders		(19.5)	(19.5)	-	-
Net cash generated from/(used by) financing activities		**558.7**	**558.7**	**102.5**	**102.5**
Net increase/(decrease) in cash and cash equivalents		327.0	326.7	(100.5)	(100.5)
Cash and cash equivalents at 1 January		450.0	450.0	550.5	550.5
Cash and cash equivalents at 31 December		**777.0**	776.7	450.0	450.0

The notes on pages 38 to 98 are an integral part of these financial statements.

Notes to the financial statements

For the year ended 31 December 2017

1. Basis of preparation

1.1 Reporting entity

Shawbrook Bank Limited is domiciled in the UK. The Company's registered office is at Lutea House, Warley Hill Business Park, The Drive, Great Warley, Brentwood, Essex, CM13 3BE. The consolidated financial statements of Shawbrook Bank Limited, for the year ended 31 December 2017, comprise the results of the Company and its subsidiaries (together referred to as the Group and individually as Group entities).

1.2 Basis of accounting

The Group's financial statements have been prepared on a historical cost basis and in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU. The financial statements are drawn up in accordance with the Companies Act 2006. No individual profit or loss account or related notes are presented for the Company as permitted by section 408 (4) of the Companies Act 2006.

1.3 Functional and presentation currency

The consolidated financial statements are presented in Pounds Sterling, which is the Company and its subsidiaries' functional currency.

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the dates of the transactions. Monetary items denominated in foreign currencies are translated at the rate prevailing at the statement of financial position reporting date. Foreign exchange gains and losses resulting from the restatement and settlement of such transactions are recognised in the statement of profit and loss. Non-monetary items (which are assets and liabilities which do not attach to a right to receive or an obligation to pay a fixed or determinable number of units of currency) denominated in foreign currencies are translated at the exchange rate at the date of the transaction.

1.4 Going concern

The financial statements are prepared on a going concern basis, as the Directors are satisfied that the Group has the resources to continue in business for at least 12 months following the year end. In making this assessment, the Directors have considered a wide range of information relating to present and future conditions, including the current state of the statement of financial position, future projections of profitability, cash flows and capital resources and the longer-term strategy of the business. The Group's capital and liquidity plans, including stress tests, have been reviewed by the Directors.

The Group's forecasts and projections suggest that it will be able to operate at adequate levels of both liquidity and capital for at least 12 months following the year end, including in a range of stressed scenarios, assuming the availability of alternative sources of capital if required and appropriate management actions.

After making due enquiries, the Directors believe that the Group has sufficient resources to continue its activities for at least 12 months following the year end, and the Group has sufficient capital to enable it to continue to meet its regulatory capital requirements as set out by the Prudential Regulation Authority.

1.5 Basis of consolidation

Subsidiaries are entities controlled by the Group. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

Entities are regarded as subsidiaries where the Group has the power over an investee, exposure or rights to variable returns from its involvement with the investee and the ability to affect those returns. Intercompany transactions and balances are eliminated upon consolidation. Subsidiaries are consolidated from the date on which control is transferred to the Group and are deconsolidated from the date that power over an investee, exposure or rights to variable returns and the ability to affect these returns ceases. Accounting policies are applied consistently across the Group.

These financial statements consolidate the results of the subsidiary companies set out in Note 31.

Basis of preparation (continued)

1.6 Critical accounting estimates and judgements
The preparation of financial statements in conformity with IFRS adopted in the EU requires Management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities at the date of the financial statements and the reported amounts of income and expenses during the reporting period. Although these estimates are based on Management's best knowledge of the amount, actual results may ultimately differ from those estimates.

The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements are disclosed within the notes to the financial statements which the estimate or judgement relates to as follows:

Area of significant judgement or estimate	Note reference
Effective interest rate	2
Impairment of loans and advances	13
Impairment assessment of goodwill	16
Customer remediation and conduct issues	22

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimates are revised and in any future periods affected.

1.7 Other reserves
Capital redemption reserve
This is a statutory, non-distributable reserve into which amounts are transferred following the redemption or purchase of a company's own shares. The provisions relating to the capital redemption reserve are set out in section 733 of the Companies Act 2006.
Merger reserve
The balance on the merger reserve represents the fair value of the consideration given in excess of the nominal value of the ordinary shares issued in acquisitions made by the issue of shares.

1.8 Reclassification of fee income
£4.2 million of fee income has been reclassified from fee and commission income to interest and similar income in order to accurately reflect the nature of the revenue. The reclassification has no effect on either the net operating income, profit before tax or the net assets of the Group.

1.9 Adoption of new and revised standards and interpretations
Minor amendments to IAS 12 'Income Taxes' and IAS 7 'Statement of Cash Flows' were adopted with effect from 1 January 2017. The adoption of these amendments had no significant impact for the Group. In all other respects, the accounting policies adopted are consistent with those of the previous financial year.

1.10 New and revised standards and interpretations not yet adopted
A number of new standards have been issued by the International Accounting Standards Board (IASB) and endorsed for use in the EU but are not effective for this financial year. The Group has not early adopted any of the new standards in preparing these consolidated financial statements.

The new standards considered to be the most relevant to the Group are as follows:

1.10.1 IFRS 9 'Financial Instruments'
IFRS 9 contains new requirements for the classification and measurement, impairment and hedge accounting of financial assets and liabilities.

In July 2014, the IASB issued the final version of IFRS 9 'Financial Instruments'. IFRS 9 is effective for annual periods beginning on or after 1 January 2018, with early adoption permitted. It replaces IAS 39 'Financial Instruments: Recognition and Measurement'.

Basis of preparation (continued)

In October 2017, the IASB issued 'Prepayment Features with Negative Compensation' (Amendments to IFRS 9). The amendments are effective for annual periods beginning on or after 1 January 2019, with early adoption permitted. The Group is not early adopting the amendments to IFRS 9.

The Group will apply IFRS 9 as issued in July 2014 initially on 1 January 2018 Based on assessments undertaken to date, the total estimated adjustment (net of tax) of the adoption of IFRS 9 on the opening balance of the Group's equity at 1 January 2018 is approximately £12.1 million, representing:

- a reduction of approximately £16.4 million related to impairment requirements (see section 1.10.1.2); and
- an increase of approximately £4.3 million related to deferred tax impacts.

The above assessment is preliminary because not all transitional work has been finalised. The actual impact of adopting IFRS 9 on 1 January 2018 may change because:

- IFRS 9 will require the Group to revise its accounting processes and internal controls and these changes are not yet complete;
- although parallel runs were carried out in the second half of 2017, the new systems and associated controls in place have not been operational for a more extended period;
- the Group has not finalised the testing and assessment of controls over its new IT systems and changes to its governance framework;
- the Group is refining and finalising its models for expected credit loss (ECL) calculations and further validations will continue into 2018; and
- the new accounting policies, assumptions, judgements and estimation techniques employed are subject to change until the Group finalises its first financial statements that include the date of initial application.

1.10.1.1 Classification and measurement – financial assets

IFRS 9 contains a new classification and measurement approach for financial assets that reflects the business model in which assets are managed and their cash flow characteristics.

IFRS 9 includes three principal classification categories for financial assets: measured at amortised cost, fair value through other comprehensive income (FVOCI) and fair value through profit and loss (FVTPL). It eliminates the existing IAS 39 categories of held to maturity, loans and receivables and available for sale.

A financial asset is measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest (SPPI) on the principal amount outstanding.

A financial asset is measured at FVOCI only if it meets both of the following conditions and is not designated as at FVTPL:

- it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets; and
- its contractual terms give rise on specified dates to cash flows that are SPPI on the principal amount outstanding.

The Group assessed the objective of the business model in which the financial assets are held at a portfolio level and concluded that, for all portfolios reviewed, management's strategy focusses on earning contractual interest revenue from the portfolios, rather than holding the portfolios for trading. For portfolios that have been sold in the past, management concluded that the sale of the portfolios were for the purposes of managing credit risk.

For the purposes of assessing whether contractual cash flows are SPPI, 'principal' is defined as the fair value of the financial asset on initial recognition. 'Interest' is defined as consideration for the time value of money, for the credit risk associated with the principal amount outstanding during a particular period of time and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a reasonable profit margin. The Group considered the contractual terms on a portfolio basis and concluded that the contractual cash flows of the portfolios are SPPI.

Basis of preparation (continued)

Impact assessment:

The Group has considered the changes in the classification and measurement criteria and has concluded that there are no significant changes in the classification and measurement of the financial assets and estimated that, on the adoption of IFRS 9 at 1 January 2018, the impact of these changes is £nil.

1.10.1.2 Impairment
IFRS 9 replaces the 'incurred loss' model in IAS 39 with a forward looking ECL model. Under IFRS 9 the measurement of the ECLs depends on the staging of the financial assets. Entities are required to recognise a 12-month ECL on initial recognition (Stage 1) and a lifetime ECL where there has been a significant increase in credit risk (Stage 2). Where there is objective evidence of impairment and the financial asset is considered to be in default, or otherwise credit impaired, then it is in Stage 3

Key accounting judgements relating to impairment

Inputs into measurement of the ECLs
The following are the key inputs into the measurement of ECLs:
- Probability of default (PD);
- Loss given default (LGD); and
- Exposure at default (EAD).

Probability of default
The Group has developed a credit grading system for all its asset classes and has aligned these to a common master grading scale that has been aligned to the Standard and Poor grading scale. The Group operates both a model based PD for its high-volume portfolios such as Consumer Lending and Secured and has developed and implemented a 'slotting approach' for the low volume and high value obligors in Development Finance, Business Finance and large ticket Commercial property cases. Both processes deliver a measure of a point-in-time measure of default.

For the model based portfolios the measure of PD is based on information available to the Group from credit reference agencies and internal product performance data. For the slotted portfolios, the measure of PD relates to attributes relating to financial strength, political and legal environment, asset/transaction characteristics, strength of sponsor and security.

For each asset class, the Group has a proprietary approach to extrapolate its best estimate of the point-in-time PD from 12 months to behavioural maturity using economic response models that have been developed specifically to forecast the sensitivity of PD to key macroeconomic variables. The Bank has used three scenarios to support its assessment of ECL. For its assessment of day one impact this includes a central view that has been used for the 2018 budget, an alternative downside base case and an alternative upside base case. These alternative base cases have been chosen to deliver a non-linearity in the final ECL number.

Loss given default
For Property portfolios, the LGD is generally broken down into two parts. These include the Group's estimate of the probability of possession given default combined with the loss given possession. The Group has continued to focus on the proportion of accounts that have not cured over an emergence period, rather than the proportion of accounts that enter possession. The LGD is based on the Group's estimate of a shortfall, based on the difference between the property value after the impact of a market value decline and sale costs, and the loan balance with the addition of unpaid interest and fees.

For Asset Finance, the LGD is based on the experience of losses on repossessed assets. The LGD on Block and Wholesale portfolios is based on experience of losses supported by key judgements.

For the Consumer portfolio, the Group uses an estimate of the probability of charge-off, defined as six or more payments in arrears, combined with an estimate of the expected write-off based on established contractual forward flow arrangements for the sale of charge-off debt.

In all cases the LGD or its components are tested against recent experience to ensure that they remain current.

Basis of preparation (continued)

Exposure at default
EAD is designed to address increases in utilisation of committed limits and unpaid interest and fees that the Group would ordinarily expect to observe to the point of default or through to the point of realisation of the collateral.

ECL is measured on either a 12-month or lifetime basis depending on whether a significant increase in credit risk has occurred since initial recognition, or whether the asset meets the definition of default.

Significant increase in credit risk (movement from Stage 1 to Stage 2):
The Group has identified a series of quantitative, qualitative and backstop criteria that will be used to determine if an account has demonstrated a significant increase in credit risk, and therefore should move from Stage 1 to Stage 2:

- quantitative measures consider the increase in an account's remaining lifetime PD at the reporting date compared to the expected residual lifetime PD when the account was originated. The Group will segment its credit portfolios into PD bands and has determined a relevant threshold for each PD band, where a movement in excess of threshold is considered to be significant. These thresholds have been determined separately for each portfolio based on historical evidence of delinquency;
- qualitative measures include the observation of specific events such as short-term forbearance, payment cancellation, historical arrears or extension to customer terms; and
- IFRS 9 includes a rebuttable presumption that 30 days past due is an indicator of a significant increase in credit risk. The Group considers 30 days past due to be an appropriate backstop measure and will not rebut this presumption.

Default (movement to Stage 3):
The Group has identified a series of quantitative and qualitative criteria that will be used to determine if an account meets the definition of default, and therefore should move to Stage 3:

- when the borrower is unlikely to pay its credit obligations to the Group in full, without recourse by the Group to actions such as realising security (if any is held);
- when the borrower is more than 90 days past due on any material credit obligation to the Group; and
- when a material credit obligation to the Group has gone past maturity or there is a degree of doubt that the exit strategy for the obligation is likely.

In assessing whether a borrower is in default, the Group will consider indicators that are:

- qualitative: e.g. breaches of covenant;
- quantitative: e.g. overdue status and non-payment of another obligation of the same issuer to the Group; and
- based on data developed internally and obtained from external sources.

The definition of default is aligned with the definition of 'credit impaired' and the regulatory definition of default.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Forward looking information:
The Group incorporates forward looking information into the assessment of significant increase in credit risk and the calculation of ECLs. The Group has identified the most significant macroeconomic factors including house price inflation, unemployment rate and Bank Base Rate.

These variables and their associated impact on PD, EAD and LGD have been factored into the ECL models. The Group has determined an approach to the selection and application of multiple scenarios. The Group does not have an in-house economics function and will therefore source economic scenarios from a third party source to form the basis of the economic scenarios used.

The ECL model will require considerable judgement over how changes in economic factors affect ECLs, which will be determined on a probability-weighted basis. The Group will consider three forward looking scenarios on a probability-weighted approach.

Basis of preparation (continued)

Impact assessment:
The most significant impact on the Group's financial statements from the implementation of IFRS 9 is expected to result from the new impairment requirements. Impairment losses will increase and become more volatile for financial instruments in the scope of the IFRS 9 impairment model.

The Group has estimated that, on the adoption of IFRS 9 at 1 January 2018, the impact of the increase in loss allowances (before tax) will be approximately £16.4 million.

1.10.1.3 Classification – financial liabilities
The classification of financial liabilities under IFRS 9 is not deemed significant as it largely retains the existing requirements in IAS 39 for the classification of financial liabilities.

1.10.1.4 Hedge accounting
When initially applying IFRS 9, the Group may choose to continue to apply the hedge accounting requirements of IAS 39 instead of the requirements in Chapter 6 of IFRS 9.

The Group has elected to continue to apply IAS 39. However, the Group will provide the expanded disclosures on hedge accounting introduced by IFRS 9's amendments to IFRS 7 'Financial Instruments: Disclosures' because the accounting policy election does not provide an exemption from these new disclosure requirements.

1.10.1.5 Disclosures
IFRS 9 will require extensive new disclosures, in particular about credit risk, ECLs and hedge accounting.

1.10.1.6 Impact on capital planning
The Group's regulator has issued guidelines on transition requirements for the implementation of IFRS 9. The guidelines allow a choice of two approaches regarding the recognition of the impact of adoption of the standard on regulatory capital:

1. phasing in the full impact on a phased basis using transitional factors published in the amended regulation EU No 575/2013; or
2. recognising the full impact on the day of adoption.

The Group has decided to adopt the first approach.

The principal impact on the Group's regulatory capital of the implementation of IFRS 9 will arise from the new impairment requirements.

Under current regulatory requirements, impairment provisions are dealt with under the standardised approach. The capital requirement is calculated based on the gross exposures net of specific provisions – i.e. net exposure. IFRS 9 is expected to increase the loss allowances associated with individual assets, and therefore the resulting net exposure and the capital requirement will fall. However, this reduction in the capital requirement will be offset by a scalar that has been published by the EU in its amended Regulation 575/2013 that aims to ensure that firms do not benefit from this impact. The Group's assessment indicates that the impact on capital resources of the implementation of IFRS 9 for the standardised portfolios will be a reduction in Common Equity Tier 1 (CET1) capital and total capital of approximately £12.1 million before adjustments for phasing in, and a reduction in CET1 capital and total capital is negligible as at 1 January 2018 after adjustments for phasing in.

1.10.1.7 Transition
The Group will record an adjustment to its opening 1 January 2018 retained earnings to reflect the application of the new requirements of IFRS 9 and will not restate comparative periods. The Group estimates the transition to IFRS 9 will reduce Shareholders' equity by approximately £12.1 million after deferred tax as at 1 January 2018.

The impact on the Group's CET1 ratio will reflect the recently published capital transitional arrangements. This adjustment arises from the increase in the Group's statement of financial position loan loss allowances as a result of the application of IFRS 9 requirements.

The Group continues to refine, monitor and validate certain elements of the impairment models and related controls ahead of full reporting of IFRS 9 impacts later in 2018.

Basis of preparation (continued)

1.10.2 IFRS 15 'Revenue from Contracts with Customers'
IFRS 15 establishes the principles to apply when reporting information about the nature, amount, timing and uncertainty of revenue and cash flows from a contract with a customer. The standard introduces a five step revenue recognition model to be applied to all contracts with customers to determine whether, how much, and when revenue is recognised.

The new standard is effective from 1 January 2018, and replaces IAS 11 'Construction Contracts', IAS 18 'Revenue', IFRIC 13 'Customer Loyalty Programmes', IFRIC 15 'Agreements for the Construction of Real Estate', IFRIC 18 'Transfers of Assets from Customers' and SIC 31 'Revenue – Barter Transactions Involving Advertising Services'. It applies to contracts with customers but does not apply to insurance contracts, financial instruments or lease contracts, which fall under the scope of other IFRSs. It also does not apply if two companies in the same line of business exchange non-monetary assets to facilitate sales to other parties.

Assessments performed to date by the Group indicate adoption of IFRS 15 will not have a material impact on the Group due to the nature of the products and services provided to clients. Assessments are ongoing to determine the impact that IFRS 15 adoption will have on a continuing basis.

Early adoption of IFRS 15 is permitted, however the Group does not intend to adopt the standard until the date it becomes effective.

1.10.3 IFRS 16 'Leases'
IFRS 16 introduces a single lessee accounting model that requires a lessee to recognise all leases (subject to certain exemptions) on-balance sheet. A lessee recognises a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. Lessor accounting is largely unchanged.

The new standard is effective from 1 January 2019 and replaces IAS 17 'Leases', IFRIC 4 'Determining whether an Arrangement Contains a Lease', SIC-15 'Operating Leases – Incentives' and SIC-27 'Evaluating the Substance of Transactions Involving the Legal Form of a Lease'. It applies to all leasing arrangements.

The Group is considering the potential impact on its consolidated financial statements. Initial assessments indicate IFRS 16 will not have a material impact as the Group is mainly a lessor of assets. Further assessments will be made to evaluate the impact that IFRS 16 adoption will have on a continuing basis. The Group has not yet decided whether it will use the optional exemptions.

Early adoption of IFRS 16 is permitted if IFRS 15 'Revenue from Contracts with Customers' has also been applied, however the Group does not intend to adopt the standard until the date it becomes effective.

1.10.4 IFRS 2 amendment 'Classification and Measurement of Share-based Payment Transactions'
In June 2016 amendments to IFRS 2 were issued in relation to the classification and measurement of share-based payment transactions. The amendments specifically relate to: effects of vesting conditions on the measurement of a cash-settled share-based payment transaction; classification of a share-based payment transaction with net settlement features for withholding tax obligations; accounting where a modification to the terms and conditions of a share-based payment transaction changes its classification from cash-settled to equity-settled.

The amendments are effective from 1 January 2018.

2. Interest and similar income

Accounting policy
Revenue represents income derived from loans and advances to customers, operating lease rentals and fees and commissions receivable.

Interest income and expense are recognised in the statement of profit and loss for all instruments measured at amortised cost using the effective interest rate method (EIRM).

The EIRM is a method of calculating the amortised cost of a financial asset or financial liability and of allocating the interest income or interest expense over the relevant period. The effective interest rate (EIR) is the rate that exactly discounts estimated future cash flows through the expected life of the financial instrument or, when appropriate, a shorter period to the net carrying amount of the financial asset or financial liability. When calculating the EIR, the Group takes into account all contractual terms of the financial instrument, for example prepayment options, but does not consider future credit losses. The calculation includes all fees paid or received between parties to the contract that are an integral part of the EIR, transaction costs and all other premiums or discounts.

Income from finance lease and instalment credit agreements is recognised over the period of the leases so as to give a constant rate of return on the net investment in the leases.

Fees and commissions which are not considered integral to the EIR are recognised on an accruals basis when the service has been provided or received.

Critical accounting estimates and judgements
Effective interest rate
IAS 39 'Financial Instruments: Recognition and Measurement' requires interest earned from loans and advances to be measured under the EIRM. Management must therefore use judgement to estimate the expected life of each instrument and hence the expected cash flows relating to it. Management reviews the expected lives on a segmental basis, whereby products of a similar nature are grouped into cohorts that exhibit homogenous behavioural attributes.

The key assumptions applied by Management in the EIR methodology are the behavioural life of the assets and the quantum of future early settlement fee income. The expected life behaviours are subjected to changes in internal and external factors and may result in adjustments to the carrying value of loans which must be recognised in the statement of profit and loss. The EIR behavioural models are based on market trends and experience. The actual behaviour of the portfolios are compared to the modelled behaviour on a quarterly basis and the modelled behaviours are adjusted if the modelled behaviour materially deviates from actual behaviour, with adjustments recognised in the statement of profit and loss.

Management continues to perform sensitivity analyses on the EIR models applied. A decrease in the redemption curve of a loan by 10% would result in a net decrease in the statement of profit and loss of £2.6 million. The movement in the sensitivity can be attributed to Property Finance and Consumer Lending. Property Finance is expected to show an income of £1.4 million mainly due to income received from early settlement fees. Consumer Lending is expected to show an expense of £3.7 million mainly attributable to the acceleration of the amortisation of broker fees.

	2017 £m	Restated[1] 2016 £m
Interest paid by customers	**307.1**	279.0
Interest received from derivative financial instruments	**4.4**	3.7
Interest on loans and advances to banks	**1.8**	1.7
Interest and similar income	**313.3**	284.4

[1] Refer to Note 1.8 for details of the restatement.

The interest income recognised during the year on loans impaired was £2.7 million (2016: £2.1 million). The Group did not capitalise any interest during the year.

3. Interest expense and similar charges

	2017 £m	2016 £m
Interest paid to depositors	**67.3**	73.0
Interest on amounts due to banks	**1.8**	1.2
Interest on subordinated debt liability	**6.4**	6.4
Other interest	**0.4**	2.4
Interest expense and similar charges	**75.9**	83.0

4. Fee and commission income

	2017 £m	Restated[1] 2016 £m
Fee income on loans and advances to customers	**10.4**	9.0
Credit facility related fees	**1.9**	2.2
Fee and commission income	**12.3**	11.2

[1] Refer to Note 1.8 for details of the restatement.

5. Administrative expenses

Accounting policy

Payroll costs

Staff costs include salaries and social security costs and are recognised over the period in which the payments relate. Cash bonus awards are recognised to the extent that the Group has a present obligation to its employees that can be measured reliably and are recognised over the period of service that employees are required to work to qualify for the payment.

The accounting policies for employee share-based payments are set out in Note 9.

Leases

If a lease agreement in which the Group is a lessee transfers the risks and rewards of the asset, the lease is recorded as a finance lease and the related asset is capitalised. At inception, the asset is recorded at the lower of the present value of the minimum lease payments or fair value and is depreciated over the estimated useful life. The lease obligations are recorded as borrowings.

If the lease does not transfer the risks and rewards of ownership of the asset, the lease is recorded as an operating lease.

Operating lease payments are charged to the statement of profit and loss on a straight-line basis over the lease term unless a different systematic basis is more appropriate. Where an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor in compensation is charged to the statement of profit and loss in the period in which termination is made.

	Notes	2017 £m	2016 £m
Payroll costs	7	**66.1**	54.1
Depreciation (excluding operating lease assets)	15	**2.6**	2.2
Amortisation of intangible assets	16	**4.0**	2.7
Operating lease rentals - land and buildings		**1.6**	1.8
Other administrative expenses		**38.9**	34.4
Administrative expenses		**113.2**	95.2

6. Auditor's remuneration

	2017 £000	2016 £000
Audit of these financial statements	**451**	408
Amounts receivable by the Company's Auditor and their associates in respect of other services:		
Audit of the financial statements of subsidiaries of the Company	**15**	15
Tax compliance services	**-**	28
Other tax advisory services	**2**	101
Audit related assurance services	**50**	30
All other assurance services	**105**	39
All other services	**33**	106
Total Auditor's remuneration	**656**	727

7. Employees

The average number of persons employed by the Group (including Directors) during the year was as follows:

	2017 No.	2016 No.
Property Finance	**143**	122
Business Finance	**133**	139
Consumer Lending	**43**	44
Central	**352**	264
Average number of employees on a full-time equivalent basis	**671**	569

The aggregate payroll costs of these persons were as follows:

	2017 £m	2016 £m
Wages and salaries	**58.0**	46.9
Social security costs	**5.6**	5.0
Pension costs	**2.5**	2.2
Total payroll costs	**66.1**	54.1

8. Employee retirement obligations

Accounting policy
The Group does not operate a defined benefit pension scheme. Pension contributions are paid to staff members' and Directors' group personal pension arrangements. The costs of the Group's contributions to such arrangements are recognised as an employee benefit expense when they are due.

The Group made contributions of £2.5 million (2016: £2.2 million) during the year.

9. Employee share-based payment transactions

Accounting policy

Where the Group engages in share-based payment transactions in respect of services received from certain of its employees, these are accounted for as equity-settled share-based payments in accordance with IFRS 2 'Share-based Payment'. The equity is in the ordinary £0.01 shares of Shawbrook Group plc.

The grant date fair value of a share-based payment transaction is recognised as an employee expense, with a corresponding increase in equity over the period that the employees become unconditionally entitled to the awards. In the absence of market prices, the fair value of the equity at the date of the grant is estimated using an appropriate valuation technique.

The amount recognised as an expense is adjusted to reflect the actual number of awards for which the related services and non-market vesting conditions are expected to be met such that the amount ultimately recognised as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.

For share-based payment awards with market performance conditions or non-vesting conditions the grant date fair value of the award is measured to reflect such conditions and there is no true-up for differences between expected and actual outcomes.

Taxation on the amount recognised as an expense is charged to the statement of profit and loss. Tax benefits of equity-settled share-based payment transactions that exceed the tax effected cumulative remuneration expenses are considered to relate to an equity item and are recognised directly in equity.

Expected volatility is determined by reviewing the share price volatility for the expected life of each option/scheme up to the date of the grant.

Cancellations of share-based payments during the vesting period are accounted for as accelerated vesting. The share-based payment is recognised immediately at the amount that would have been recognised for services received over the remainder of the vesting period, as if the service and the non-market performance conditions were met for the cancelled awards.

Critical accounting estimates and judgements

Critical accounting estimates and judgements have been discussed below within the various categories of share-based payments.

The employee share-based payment charge comprises:

	2017 £m	2016 £m
Save-as-you-earn schemes (SAYE)	**0.8**	0.1
Performance share plan (PSP) – 2015	**1.4**	1.6
Performance share plan (PSP) – 2016	**1.7**	3.1
Performance share plan (PSP) – 2017	**2.4**	-
Deferred share bonus plan (DSBP) – 2017	**1.2**	-
Share-based payments	**7.5**	4.8

Employee share-based payment transactions (continued)

Movements in the number of share-based awards are as follows:

No. of shares	**DSBP 2017**	SAYE 2016	SAYE 2015	**PSP 2017**	PSP 2016	PSP 2015	**Total**
At 1 January 2017	-	1,298,794	160,095	-	1,792,612	1,277,471	**4,528,972**
Granted	**301,615**	-	-	**1,547,183**	-	-	**1,848,798**
Vested	**(301,615)**	(245,361)	(123,108)	**(269,706)**	(1,089,905)	(962,750)	**(2,992,445)**
Lapsed	-	(1,053,433)	(36,987)	**(1,277,477)**	(702,707)	(314,721)	**(3,385,325)**
At 31 December 2017	-	-	-	-	-	-	-

Accelerated vesting of the schemes
Subsequent to the acquisition of Shawbrook Group plc by Marlin Bidco Limited, there was an issue of 2,586,879 £0.01 shares in Shawbrook Group plc and the vesting of all share option schemes was accelerated. The acceleration of the share options is recognised as if the service and the non-market performance conditions of all schemes were met. Subsequent to vesting, all shares were repurchased by Marlin Bidco Limited at the offer price of £3.40. The total acceleration charge of £5.9m is included in the total charge of £7.5m.

Prior to the acquisition, the following schemes were granted (and subsequently accelerated):

Deferred share bonus plan (DSBP) – 2017 plan
During March 2017, 301,615 awards were granted to selected members of senior management of which the share price at grant date was £3.14. The scheme was deemed to be an equity-settled scheme and has been accounted for as such in the financial statements of the Group. Each award was structured as a nil cost option with no performance conditions attached, although the individuals were subject to continued employment until March 2020.

Save-As-You-Earn schemes (SAYE) – 2015 and 2016
In October 2015, the Save-As-You-Earn scheme was introduced for all employees. The scheme provided employees with the opportunity to take part in a tax efficient savings scheme and to acquire Shawbrook Group plc shares at a discount to market value. The shares subject to this option had no restrictions, save those restrictions applying as a matter of law, regulation and the Company's dealing code. The SAYE scheme was governed by the Company's Articles of Association. The scheme was deemed by Management to be an equity-settled scheme and has been accounted for as such in the financial statements of the Group. The fair value of the call options was calculated as £0.71. The awards generally required employees to remain in employment over the vesting period but were not subject to performance conditions after the grant date. The awards vested over a period of three years.

In October 2016, a further SAYE scheme was introduced for all employees. The scheme's terms and conditions were the same as those of the 2015 scheme. The fair value of the call options for this scheme was calculated as £0.66. The awards vested over a period of three years.

The call options were valued using the Black-Scholes valuation model. The assumptions used were as follows:

Assumptions	2016 Scheme	2015 Scheme
Share price at grant date	£2.48	£3.10
Expected volatility	30.80%	25.90%
Dividend yield	3.31%	2.08%
Risk-free rate of return	0.19%	0.74%
Weighted average contractual life (years) at grant date	3.17	3.17
Exercise price	£1.87	£2.60

Employee share-based payment transactions (continued)

Performance Share Plan (PSP) – 2017 plan
During 2017, 1,547,183 share awards were granted to a set of individuals. These individuals were entitled to acquire ordinary shares in Shawbrook Group plc, subject to performance conditions. The scheme was deemed to be an equity-settled scheme and has been accounted for as such in the financial statements of the Group.

The performance conditions for the 2017 tranche related to the growth in total shareholder return (TSR) over the vesting period for 20% of each award, the customer and employee performance condition (CEP) at the date of vesting for 20% of each award, the risk performance over the vesting period for 20% of each award and the annual compound growth in the earnings per share (EPS) over the vesting period for 40% of each award. The outcome of the performance conditions, as assessed by the Remuneration Committee, determined the vesting outcome of the awards and the shares available for exercise.

The performance condition relating to the TSR element was measured in relation to the ranking of the Group's TSR within a comparator group of companies selected by the Remuneration Committee.

The fair value of the shares in the EPS, CEP and risk performance elements of the awards was based on the share price at the date of the grant. The fair value of these awards was £2.94.

The fair value of the shares in the TSR award was calculated using a Monte Carlo model. Set out below is a summary of the key data and assumptions used to calculate the fair value of the TSR award:

Assumptions	
Share price at grant date	**£3.14**
Expected volatility	**35% p.a.**
Dividend yield	**2.50% p.a.**
Risk-free rate of return	**0.16% p.a.**

The fair value of the shares in the TSR award was £1.89.

Performance Share Plan (PSP) – 2016 plan
During 2016, 2,181,165 share awards were granted to a set of individuals. These individuals were entitled to acquire ordinary shares in Shawbrook Group plc, subject to performance conditions. The scheme was deemed to be an equity-settled scheme and has been accounted for as such in the financial statements of the Group. This amount included a number of options related to new hires as discussed below in 'New hires – 2016'.

The performance conditions for the 2016 tranche related to the growth in total shareholder return (TSR) over the vesting period for 20% of each award, the net promotor score (NPS) at the date of vesting for 20% of each award, the risk performance over the vesting period for 20% of each award and the annual compound growth in the earnings per share (EPS) over the vesting period for 40% of each award. The outcome of the performance conditions, as assessed by the Remuneration Committee, determined the vesting outcome of the awards and the shares available for exercise.

The performance condition relating to the TSR element was measured in relation to the ranking of the Group's TSR within a comparator group of companies selected by the Remuneration Committee.

The fair value of the shares in the EPS, NPS and risk performance elements of the awards was based on the share price at the date of the grant discounted for any expected dividends over the vesting period. The dividend adjusted fair value of these awards was £2.63.

Employee share-based payment transactions (continued)

The fair value of the shares in the TSR award was calculated using a Monte Carlo model with 100,000 simulations. Set out below is a summary of the key data and assumptions used to calculate the fair value of the TSR award:

Assumptions	
Share price at grant date	£2.87
Expected volatility	30% p.a.
Dividend yield	2.83% p.a.
Risk-free rate of return	0.51% p.a.

The fair value of the shares in the TSR award was £1.46.

Performance Share Plan (PSP) – 2015 plan
During 2015 a number of share awards were granted to a set of individuals other than Directors. These individuals were entitled to receive an award to acquire a specific number of ordinary shares in Shawbrook Group plc, subject to performance conditions. The scheme was deemed to be an equity-settled scheme and has been accounted for as such in the financial statements of the Group. The share awards were subject to performance conditions, namely the Group earning a defined underlying profit before tax in 2017, and subject to the Group maintaining its threshold capital and liquidity requirements.

The fair value of the shares was based on the share price at the dates of the grant discounted for any expected dividends over the vesting period. The weighted average fair value of the shares issued was £3.25.

New hires – 2016
During 2016 a number of senior hires were, under the terms of their employment with the Group, granted options over shares of £0.01 in Shawbrook Group plc, in accordance with the 'Performance Share Plan - 2016 plan' discussed above, in order to compensate them for forfeited awards from previous employment. A total of 897,403 options were granted that vested over the following two years.

10. Directors' remuneration

	2017	2016
	£000	£000
Directors' emoluments	**5,285.3**	3,328.9
Contributions to money purchase scheme	**-**	13.0
Directors' remuneration	**5,285.3**	3,341.9

Included in the current year Directors' emoluments is £nil (2016: £1.1 million) relating to new hires (refer to Note 10 for more information) and £nil (2016: £228,000) relating to termination payments.

11. Taxation

Accounting policy
Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the statement of profit and loss except to the extent that it relates to items recognised directly in equity, in which case it is recognised in equity.

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

Recognised in the statement of profit and loss	2017 £m	2016 £m
Current tax:		
Current year	**24.2**	27.4
Adjustment in respect of prior years	**(1.1)**	(0.2)
Total current tax	**23.1**	27.2
Deferred tax:		
Origination and reversal of temporary difference	**1.3**	(4.0)
Adjustment in respect of prior years	**0.9**	0.2
Total deferred tax	**2.2**	(3.8)
Total tax charge	**25.3**	23.4

Tax reconciliation	2017 £m	2016 £m
Profit before tax	**99.5**	89.1
Implied tax charge thereon at 19.25% (2016: 20%)	**19.2**	17.8
Adjustments:		
Banking surcharge	**5.1**	5.4
Prior year adjustment	**(0.2)**	-
Disallowable expenses and other permanent differences	**1.2**	0.2
Total tax charge	**25.3**	23.4

Reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and further reductions to 17% (effective 1 April 2020) were substantively enacted on 16 March 2016. This will reduce the Company's future current tax charge accordingly.

The deferred tax asset at 31 December 2017 has been calculated based on an aggregation of a rate of 18% substantively enacted at the statement of financial position reporting date and the additional 8% of tax suffered in relation to the banking surcharge that will unwind over the remaining life of the underlying assets with which they are associated.

12. Loans and advances to customers

Accounting policy
Loans and advances
The Group's loans and advances to banks and customers are classified as loans and receivables. Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, whose recoverability is based solely on the credit risk of the customer and where the Group has no intention of trading the loan or receivable. Loans and receivables are initially recognised at fair value including direct and incremental transaction costs. Subsequent recognition is at amortised cost using the effective interest rate method, less any provision for impairment.

Assets acquired in exchange for loans
Included within loans and advances to customers are assets acquired in exchange for loans, instalment credit and finance lease receivables as part of an orderly realisation. The asset acquired is recorded at the lower of its fair value (less costs to sell) and the carrying amount of the lease (net of impairment allowance) at the date of exchange. Any subsequent write-down of the acquired asset to fair value less costs to sell is recognised in the statement of profit and loss. Any subsequent increase in the fair value less costs to sell, to the extent this does not exceed the cumulative write-down, is also recognised in the statement of profit and loss, together with any realised gains or losses on disposal.

Loans and advances to customers include those classified as loans and advances, finance leases and instalment credit advances as summarised below:

	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Loan receivables	**4,418.7**	**4,413.8**	3,639.5
Finance lease receivables	**79.8**	**79.8**	93.6
Instalment credit receivables	**348.0**	**307.9**	316.9
Fair value adjustments for hedged risk	**(2.2)**	**(2.2)**	0.4
Total loans and advances to customers	**4,844.3**	**4,799.3**	4,050.4

At 31 December 2017, loans and advances to customers of £1,081.7 million (2016: £695.2 million) were positioned with the Bank of England for use as collateral under its funding schemes.

Loan receivables	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Gross loan receivables	**4,438.4**	**4,433.5**	3,653.1
Less: allowances for impairment losses	**(19.7)**	**(19.7)**	(13.6)
Net loan receivables	**4,418.7**	**4,413.8**	3,639.5

The Group provides finance lease and instalment credit agreements to customers for a variety of assets including plant and machinery, taxis, aviation and marine vessels. These assets provide security against the gross receivables. Included within instalment credit receivables are block discounting facilities of £106.6 million (2016: £107.5 million).

Loans and advances to customers (continued)

Finance lease receivables	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Gross amounts receivable			
within one year	**47.0**	**47.0**	59.5
in the second to fifth year inclusive	**49.5**	**49.5**	55.2
after five years	**3.0**	**3.0**	1.5
	99.5	**99.5**	116.2
Less: unearned finance income	**(10.6)**	**(10.6)**	(14.1)
Less: allowances for impairment losses	**(9.1)**	**(9.1)**	(8.5)
Net investment in finance lease receivables	**79.8**	**79.8**	93.6
Amounts falling due			
within one year	**37.5**	**37.5**	47.1
in the second to fifth year inclusive	**39.7**	**39.7**	45.2
after five years	**2.6**	**2.6**	1.3
Net investment in finance lease receivables	**79.8**	**79.8**	93.6

Instalment credit receivables	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Gross amounts receivable			
within one year	**162.5**	148.4	165.9
in the second to fifth year inclusive	**204.9**	183.9	182.6
after five years	**18.1**	10.2	6.6
	385.5	342.5	355.1
Less: unearned finance income	**(34.7)**	(31.9)	(35.9)
Less: allowances for impairment losses	**(2.8)**	(2.7)	(2.3)
Net investment in instalment credit receivables	**348.0**	307.9	316.9
Amounts falling due			
within one year	**143.3**	130.2	143.3
in the second to fifth year inclusive	**186.8**	167.3	167.3
after five years	**17.9**	10.4	6.3
Net investment in instalment credit receivables	**348.0**	307.9	316.9

Cost of equipment acquired during the year	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Finance leases	**40.1**	40.1	43.9
Instalment credit	**161.5**	120.8	128.7
Total cost of equipment acquired during the year	**201.6**	160.9	172.6

13. Impairment provisions on loans and advances to customers

Accounting policy

On an ongoing basis, the Group assesses whether there is objective evidence that a financial asset or group of financial assets is impaired. A financial asset or a group of financial assets is impaired and impairment losses are incurred if, and only if, there is objective evidence of impairment as a result of one or more events that occurred after the initial recognition of the asset (a 'loss event') and that loss event (or events) has an impact on the estimated future cash flows of the financial asset or group of financial assets that can be reliably estimated.

The criteria that the Group uses to determine that there is objective evidence of an impairment loss include, but are not limited to, the following:

delinquency in contractual payments of principal or interest;
cash flow difficulties experienced by the borrower;
initiation of bankruptcy proceedings;
the customer being granted a concession that would otherwise not be considered; and
observable data indicating that there is a measurable decrease in the estimated future cash flows from a portfolio of assets since the initial recognition of those assets, although the decrease cannot yet be identified with the individual financial assets in the portfolio.

If there is objective evidence that an impairment loss on an individual financial asset has occurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the financial asset's original effective interest rate. The carrying amount of the asset is reduced through the use of an allowance account and the amount of the loss is recognised in the statement of profit and loss. If a loan has a variable interest rate, the discount rate for measuring any impairment loss is the current effective interest rate determined under the contract.

If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Objective evidence of impairment of a portfolio of receivables exists if objective data indicates a decrease in expected future cash flows from a collection of receivables and the decrease can be measured reliably but cannot be identified with the individual receivables in the portfolio in which case a collective provision is applied.

When a loan or receivable is not economic to recover, it is written off against the related provision for loan impairments. Such loans are written off after all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off are recognised directly in the statement of profit and loss through the impairment line as post write-off recoveries. If, in a subsequent period, the amount of impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised (such as an improvement in the customer's credit rating), the previously recognised impairment loss is reversed by adjusting the impairment allowance. The amount of reversal is recognised in statement of profit and loss.

The Group operates a forbearance policy in situations where it becomes aware that an individual customer is experiencing financial hardship. Repayment options are discussed with the customer that are appropriate to the customer's specific situation. The Group seeks to ensure that any forbearance results in a fair customer outcome and will not repossess an asset unless all other reasonable attempts to resolve the position have failed. Further information is provided in Note 30.1.1.

Impairment provisions on loans and advances to customers (continued)

Critical accounting estimates and judgements
Individual impairment losses on loans and advances are calculated based on an assessment of the expected cash flows and the underlying collateral. For individual provisions, statistical models are used for consumer and second charge loans, whilst provisions for first charge loans, asset finance and business finance are assessed on a loan-by-loan basis. Where models are used for individual provisions, score cards are used to calculate probability of default (PDs) based on the recent performance of the portfolios. Loss given defaults (LGDs) are calculated taking into account the valuations of available collateral, and the experienced forced sale discounts when collateral has been realised. These factors are applied to all the aged portfolios of debt at each statement of financial position reporting date to derive the individual impairment requirement.

For the purpose of collective impairment, financial assets are grouped on the basis of similar risk characteristics. For some portfolios, the collective impairment requirement is based on the forecast cost of risk, being the annualised percentage loss per monetary unit of loan across the loan portfolios. These loss rates are multiplied by emergence periods, currently six months for all portfolios (2016: six months), for each class of loan to calculate the amount of loss which is incurred at the statement of financial position reporting date but not yet individually identified.

The key assumptions, being the emergence periods, forced sale discount (FSD) on the Residential portfolio, cost of risk and PD of the Residential and Consumer portfolios, are monitored regularly to ensure the impairment allowance is entirely reflective of the current portfolio. The accuracy of the impairment calculation would therefore be affected by unanticipated changes to the economic situation and assumptions which differ from actual outcomes. For example, for loans and advances:

change of one month in the emergence period across all portfolios, would change the collective provision by £1.5 million (2016: £0.9 million);

a change in the cost of risk rate of 10 basis points, would change the collective provision by £2.2 million (2016: £1.7 million);

an increase in the forced sale discount on the Residential portfolio of 5%, would increase the individual provisions by £0.8 million (2016: £0.5 million); and

an increase in the PD on the Residential and Consumer portfolios of 10%, would increase the individual provisions by £2.4 million (2016: £1.1 million).

The movement in the allowances for losses in respect of loans, finance leases and instalment credit agreements during the year was as follows:

	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
At 1 January	**24.4**	**24.4**	13.5
Charge for impairment losses	**23.3**	**23.2**	24.3
Amounts written off in the year	**(18.6)**	**(18.6)**	(15.2)
Amounts recovered in the year	**2.5**	**2.5**	1.8
At 31 December	**31.6**	**31.5**	24.4
Analysis of impairment type:			
Loan receivables	**19.7**	**19.7**	13.6
Finance lease receivables	**9.1**	**9.1**	8.5
Instalment credit receivables	**2.8**	**2.7**	2.3
At 31 December	**31.6**	**31.5**	24.4

14. Derivative financial instruments

Accounting policy

Derivatives and hedge accounting

The Group's derivative activities are entered into for the purposes of matching or eliminating risk from potential movements in interest rates and foreign exchange in the Group's assets and liabilities. Derivatives which are not designated as hedging instruments in qualifying hedge relationships are used to manage the Bank's exposure to interest rate and foreign exchange risk.

The Group uses interest rate swaps and options to hedge its interest rate risks. Such derivative financial instruments are initially recognised at fair value on the date on which the derivative contract is entered into and are subsequently remeasured at fair value.

Fair values are obtained from quoted market prices in active markets and, where these are not available, from valuation techniques including discounted cash flow models (at a benchmark interest rate, typically OIS or its equivalent) and option pricing models.

Derivatives are measured as assets where their fair value is positive and liabilities where their fair value is negative. The Group applies the exemption under IFRS 9 'Financial Instruments' to continue to apply the hedge accounting rules as per IAS 39 'Financial Instruments: Recognition and Measurement', and as such all hedge relationships must be clearly and formally documented at inception and the derivative must be expected to be highly effective at mitigating the hedged risk.

The Group undertakes transactions denominated in foreign currencies; consequently, exposures to exchange rate fluctuations arise. Exchange rate exposures are managed within approved policy parameters utilising forward foreign exchange contracts.

Fair value hedge

The change in the fair value of a hedging instrument is recognised in the statement of profit and loss. The change in the fair value of the hedged item attributable to the risk hedged is recorded as part of the carrying value of the hedged item and is also recognised in the statement of profit and loss. Where hedging gains/losses are recognised in the statement of profit and loss they are recognised on the same line as the hedged item. The Group discontinues hedge accounting only when the relationship (or a part thereof) ceases to meet the qualifying criteria. This includes when the hedging instrument is sold or expires. The fair value adjustment to the carrying amount of the hedged item, for which the EIR method is used, arising from the hedged risk is amortised to the statement of profit and loss commencing no later than the date when hedge accounting is discontinued.

Unobservable valuation differences on initial recognition

The transaction price in the market in which derivative transactions are undertaken may be different from the fair value of the derivative transaction. On initial recognition, the fair value will be adjusted to bring it in line with the transaction price (i.e. day 1 profit or loss will be deferred by including it in the initial carrying amount of the asset or liability).

Derivative financial instruments (continued)

Derivatives held for risk management
The Group uses derivatives to reduce exposure to market risks, and not for trading purposes. The Group uses the International Swaps and Derivatives Association (ISDA) Master Agreement to document these transactions in conjunction with a Credit Support Annex (CSA). The following table, prepared under IAS 39, analyses derivatives held for risk management purposes by type of instrument:

	Notional Amount £m	Fair Value £m
Interest rate swaps:		
Assets	**389.0**	**1.8**
Liabilities	**189.0**	**(0.3)**
Interest rate options:		
Liabilities	**500.0**	**(2.8)**
Foreign exchange swaps:		
Liabilities	**20.7**	**(0.3)**
At 31 December 2017	**1,111.3**	**(1.6)**
Interest rate swaps:		
Assets	485.0	5.2
Liabilities	39.0	(0.4)
Foreign exchange swaps:		
Liabilities	16.4	-
At 31 December 2016	540.4	4.8

Gains and losses from derivatives and hedge accounting are as follows:

	2017 £m	2016 £m
Fair value gain on financial instruments	**3.9**	2.0
Fair value loss on hedged risk	**(3.7)**	(1.5)
Fair value gain on financial instruments	**0.2**	0.5

It is the Group's policy to enter into master netting and margining agreements with all derivative counterparties. In general, under master netting agreements the amounts owed by each counterparty that are due on a single day in respect of all transactions outstanding under the agreement are aggregated into a single net amount payable by one party to the other. In certain circumstances, for example when a credit event such as a default occurs, all outstanding transactions under the agreement are aggregated into a single net amount payable by one party to the other and the agreements terminated.

Under margining agreements where the Group has a net asset position valued at current market values, in respect of its derivatives with a counterparty, then that counterparty will place collateral, usually cash, with the Group in order to cover the position. Similarly, the Group will place collateral, usually cash, with the counterparty where it has a net liability position.

The Group's property loan portfolio includes loans whose interest rate terms are referenced to the three-month LIBOR index, but with a minimum reference rate of 0.75%. On 29 March 2017, the Group sold interest rate options with a nominal value of £500 million into the wholesale market in order to hedge the Group's interest rate position against possible increases in the reference rate.

Derivative financial instruments (continued)

The table below illustrates the amounts that are covered by enforceable netting arrangements (i.e. offsetting agreements and any related financial collateral). The table excludes financial instruments not subject to offset and those that are subject to collateral arrangements only (e.g. loans and advances).

	Amounts subject to enforceable netting arrangements					
	Effect of offsetting on statement of financial position			Related amounts not offset		
	Gross amount £m	Amount offset %	Net amount reported on statement of financial position £m	Cash collateral £m	Net amount £m	Amount not subject to enforceable netting arrangements £m
At 31 December 2017						
Derivative financial instruments - assets	**1.8**	**-**	**1.8**	**1.8**	**-**	**-**
Derivative financial instruments - liabilities	**(3.4)**	**-**	**(3.4)**	**(3.4)**	**-**	**-**
Total financial instruments	**(1.6)**	**-**	**(1.6)**	**(1.6)**	**-**	**-**
At 31 December 2016						
Derivative financial instruments - assets	5.2	-	5.2	5.2	-	-
Derivative financial instruments - liabilities	(0.4)	-	(0.4)	(0.4)	-	-
Total financial instruments	4.8	-	4.8	4.8	-	-

Collateral amounts (cash and non-cash financial collateral) are reflected at their fair value; however, this amount is limited to the net statement of financial position exposure in order not to include any over-collateralisation.

Details of derivatives designated as hedging instruments in qualifying hedging relationships are provided under 'Hedge accounting' below.

Hedge accounting

Fair value hedges of interest rate risk and foreign currency risk

The Group uses interest rate swaps and cross currency swaps to hedge its exposure to changes in the fair values of fixed rate loans and advances to customers in respect of a benchmark interest rate (mainly three-month LIBOR) and foreign currency risks (mainly Euro and US Dollar). Interest rate swaps are matched to specific issuances of fixed rate loans.

The Group's approach to managing market risk, including interest rate risk and foreign currency risk is discussed in Note 31. The Group hedges interest rate risk only to the extent of benchmark interest rates. The benchmark interest rate is a component of interest rate risk that is observable in the relevant environments. Hedge accounting is applied where economic hedge relationships meet the hedge accounting criteria.

The Group does not apply a credit valuation adjustment (CVA) or debit valuation adjustment (DVA) as the Group's portfolio is fully collateralised. The Group does not apply funding fair value adjustment (FFVA) to its derivative exposures as it deems the adjustment to be immaterial.

When fair value hedge accounting is applied by the Group, the Group assesses whether the derivative designated in each hedge relationship is expected to be and has been highly effective in offsetting the changes in fair value of the hedged item using linear regression.

Derivative financial instruments (continued)

Under the Group policy, in order to conclude that a hedge relationship is effective, all of the following criteria should be met:

- >There is a formal designation and written documentation at the inception of the hedge.
- >The effectiveness of the hedging relationship can be measured reliably. This requires the fair value of the hedging instrument, and the fair value of the hedged item with respect to the risk being hedged, to be reliably measurable.
- >The hedge is expected to be highly effective in achieving fair value offsets in accordance with the original documented risk management strategy.
- >The hedge is assessed and determined to be highly effective if changes in the fair value of the hedging instrument, and changes in the fair value or expected cash flows of the hedged item attributable to the hedged risk, offset within the range of 80-125%.

In these hedge relationships, the main sources of ineffectiveness relates to the modelled prepayment behaviour and the assumptions that are used in modelling this behaviour. There were no other sources of ineffectiveness in these hedge relationships.

Fair value gains on derivatives held in qualifying fair value hedging relationships and the hedging gain or loss on the hedged items are included in net interest income.

At 31 December 2017, the Group held the following interest rate swaps as hedging instruments in fair value hedges:

At 31 December 2017	Less than 1 month	1-3 months	3 months - 1 year	1-5 years	Maturity More than 5 years
Interest rate risk:					
Nominal amount (£m)	-	-	307.0	740.0	31.0
Average fixed interest rate	-	-	1.17%	1.16%	0.94%

Fair value hedges
The amounts relating to items designated as hedging instruments and hedge ineffectiveness were as follows:

At 31 December 2017	Nominal amount £m	Carrying amount Asset £m	Carrying amount Liabilities £m	Statement of financial position line item	Change in fair value used for calculating hedge ineffectiveness £m	Ineffectiveness recognised in statement of profit and loss £m	Statement of profit and loss line item
Interest rate risk:							
Interest rate swaps	389.0	1.8	-	Derivative financial assets	-	-	-
Interest rate swaps	189.0	-	(0.3)	Derivative financial liabilities	(0.7)	0.1	Fair value gains on financial instruments
Interest rate options	500.0	-	(2.8)	Derivative financial liabilities	4.6	0.1	Fair value gains on financial instruments

Derivative financial instruments (continued)

The amounts relating to items designated as hedged items were as follows:

At 31 December 2017	Carrying amount Assets £m	Carrying amount Liabilities £m	Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item Assets £m	Accumulated amount of fair value hedge adjustments on the hedged item included in the carrying amount of the hedged item Liabilities £m	Statement of financial position line item	Change in value used for calculating hedge ineffectiveness £m	Accumulated amount of fair value hedge adjustments £m
Loans and advances to customers	1,227.1	-	4.1	-	Loans and advances to customers	(3.7)	(3.7)
Customer deposits	-	407.0	-	(1.9)	Customer deposits	-	0.5

15. Property, plant and equipment

Accounting policy

Operating leases

Included within property, plant and equipment are assets leased to customers under operating leases. The net book value of operating leases represents the original cost of the equipment less cumulative depreciation. Rentals are recognised on a straight-line basis over the lease term. Depreciation is recognised on a straight-line basis to a residual value over the life of the associated agreement.

Depreciation

Tangible fixed assets are stated at historical cost less accumulated depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items.

Depreciation is charged to the statement of profit and loss on a straight-line basis over the estimated useful lives of each part of an item of plant and equipment as follows:

office equipment	3/5 years
fixtures and fittings	10 years
motor vehicles	4 years
freehold property	50 years
leasehold costs	life of the lease
operating leases[1]	life of the lease

[1] Operating leases are assets leased to customers.

Depreciation methods, useful lives and residual values are reviewed at each statement of financial position reporting date.

Assets acquired in exchange for operating leases

Included within property, plant and equipment are assets acquired in exchange for operating leases as part of an orderly realisation. The asset acquired is recorded at the lower of its fair value (less costs to sell) and the carrying amount of the lease (net of impairment allowance) at the date of exchange. No depreciation is charged in respect of assets held for sale. Any subsequent write-down of the acquired asset to fair value less costs to sell is recognised in the statement of profit and loss. Any subsequent increase in the fair value less costs to sell, to the extent it does not exceed the cumulative write-down, is also recognised in the statement of profit and loss, together with any realised gains or losses on disposal.

Residual values

The residual values of assets under operating leases are reviewed by Management for impairment, taking into account the nature and condition of the assets. Where the residual value of the assets exceeds the estimated recoverable amount, the assets are impaired and the impairment charged to the statement of profit and loss.

Property, plant and equipment (continued)

Group	Freehold property £m	Leasehold property £m	Fixtures, fittings & equipment £m	Assets on operating leases £m	Total £m
Cost					
At 1 January 2016	0.2	0.1	10.2	67.3	77.8
Additions	-	-	0.2	11.1	11.3
Disposals	(0.2)	-	-	(11.2)	(11.4)
Transfer to finance leases	-	-	-	(10.6)	(10.6)
At 31 December 2016	-	0.1	10.4	56.6	67.1
Additions	**-**	**0.7**	**0.9**	**11.7**	**13.3**
Disposals	**-**	**-**	**(0.1)**	**(7.8)**	**(7.9)**
Transfer to finance leases	**-**	**-**	**-**	**(8.7)**	**(8.7)**
At 31 December 2017	**-**	**0.8**	**11.2**	**51.8**	**63.8**
Depreciation					
At 1 January 2016	-	0.1	3.7	25.4	29.2
Depreciation charge for the year	-	-	2.2	11.3	13.5
Disposals	-	-	-	(9.9)	(9.9)
Transfer to finance leases	-	-	-	(8.3)	(8.3)
At 31 December 2016	-	0.1	5.9	18.5	24.5
Depreciation charge for the year	**-**	**0.4**	**2.2**	**10.6**	**13.2**
Disposals	**-**	**-**	**(0.1)**	**(6.3)**	**(6.4)**
Transfer to finance leases	**-**	**-**	**-**	**(7.1)**	**(7.1)**
At 31 December 2017	**-**	**0.5**	**8.0**	**15.7**	**24.2**
Net book value					
At 31 December 2016	-	-	4.5	38.1	42.6
At 31 December 2017	**-**	**0.3**	**3.2**	**36.1**	**39.6**

Property, plant and equipment (continued)

Company	Freehold property £m	Leasehold property £m	Fixtures, fittings & equipment £m	Assets on operating leases £m	Total £m
Cost					
At 1 January 2016	0.2	0.1	10.2	67.3	77.8
Additions	-	-	0.2	11.1	11.3
Disposals	(0.2)	-	-	(11.2)	(11.4)
Transfer to finance leases	-	-	-	(10.6)	(10.6)
At 31 December 2016	-	0.1	10.4	**56.6**	**67.1**
Additions	**-**	**0.7**	**0.9**	**11.3**	**12.9**
Disposals	**-**	**-**	**(0.1)**	**(7.8)**	**(7.9)**
Transfer to finance leases	**-**	**-**	**-**	**(8.7)**	**(8.7)**
At 31 December 2017	**-**	**0.8**	**11.2**	**51.4**	**63.4**
Depreciation					
At 1 January 2016	-	0.1	3.7	25.8	29.6
Depreciation charge for the year	-	-	2.2	10.9	13.1
Disposals	-	-	-	(9.9)	(9.9)
Transfer to finance leases	-	-	-	(8.3)	(8.3)
At 31 December 2016	-	0.1	5.9	**18.5**	**24.5**
Depreciation charge for the year	**-**	**0.4**	**2.2**	**10.6**	**13.2**
Disposals	**-**	**-**	**(0.1)**	**(6.3)**	**(6.4)**
Transfer to finance leases	**-**	**-**	**-**	**(7.1)**	**(7.1)**
At 31 December 2017	**-**	**0.5**	**8.0**	**15.7**	**24.2**
Net book value					
At 31 December 2016	-	-	4.5	38.1	42.6
At 31 December 2017	**-**	**0.3**	**3.2**	**35.7**	**39.2**

16. Intangible assets

Accounting policy

Goodwill

Goodwill may arise on the acquisition of subsidiaries and represents the excess of the aggregate of the fair value of consideration transferred and the fair value of any non-controlling interest over the fair value of identifiable net assets at the date of acquisition. Goodwill is stated at cost less any accumulated impairment losses.

Goodwill is not amortised but is tested annually for impairment and additionally whenever there is an indication that impairment may exist. For the purpose of impairment testing, goodwill is allocated to cash generating units (CGUs). A CGU is the smallest identifiable group of assets that generates cash inflows that are largely independent of the cash inflows from other assets or groups of assets. An impairment loss is recognised if the carrying amount of a CGU exceeds its recoverable amount. Recoverable amount is the greater of the CGUs value in use and fair value less costs to sell. Value in use is based on estimated future cash flows less a residual value, discounted at a risk-adjusted discount rate appropriate to the CGU. Where impairment is required, the amount is recognised in the statement of profit and loss and cannot subsequently be reversed.

Computer software

Computer software acquired by the Group is stated at cost less accumulated amortisation and any accumulated impairment losses.

Internally developed computer software is recognised as an asset only when the Group is able to demonstrate that the following conditions have been met: expenditure can be reliably measured, the product or process is technically and commercially feasible, future economic benefits are probable, and, the Group has the intention and ability to complete development and subsequently use or sell the asset. If these conditions are not met, expenditure is recognised in the statement of profit and loss as incurred. Capitalised costs include all costs directly attributable to developing the computer software. Internally developed computer software is stated at capitalised cost less accumulated amortisation and any accumulated impairment losses.

Subsequent expenditure on software assets is capitalised only when it increases the future economic benefits embodied in the specific asset to which it relates. All other expenditure is recognised in the statement of profit and loss as incurred.

Computer software is amortised on a straight-line basis over its estimated useful life from the date it is available for use. The estimated useful life of computer software is between three and seven years. Amortisation is recognised in the statement of profit and loss. The amortisation method, useful lives and residual values are reviewed at each reporting date and adjusted if appropriate.

Critical accounting estimates and judgements

The review of goodwill for impairment reflects Management's best estimate of future cash flows of the CGUs and the rates used to discount these cash flows, both of which are subject to judgement and uncertainty as follows:

> the future cash flows of the CGUs are sensitive to projected cash flows based on the forecasts and assumptions regarding the projected periods and the long-term pattern of sustainable cash flows thereafter.

> the rates used to discount future expected cash flows can have a significant effect on their valuations and are based on the price-to-book ratio method which incorporates inputs reflecting a number of variables. These variables are subject to uncertainty and require the exercise of significant judgement.

Intangible assets (continued)

The factors and inputs are described in more detail below.

Group	Goodwill £m	Computer software £m	Total £m
At 1 January 2016	38.5	9.9	48.4
Additions	-	7.9	7.9
Amortisation	-	(2.7)	(2.7)
At 31 December 2016	38.5	15.1	53.6
At 1 January 2017	**38.5**	**15.1**	**53.6**
Additions	**-**	**9.8**	**9.8**
Amortisation	**-**	**(4.0)**	**(4.0)**
At 31 December 2017	**38.5**	**20.9**	**59.4**

Company	Goodwill £m	Computer software £m	Total £m
At 1 January 2016	23.7	9.9	33.6
Additions	-	7.9	7.9
Amortisation	-	(2.7)	(2.7)
At 31 December 2016	23.7	15.1	38.8
At 1 January 2017	**23.7**	**15.1**	**38.8**
Additions	**-**	**9.8**	**9.8**
Amortisation	**-**	**(4.0)**	**(4.0)**
At 31 December 2017	**23.7**	**20.9**	**44.6**

Total cost of computer software amounted to £29.1 million (2016: £19.3 million) while accumulated amortisation amounted to £8.2 million (2016: £4.2 million). Additions of £9.8 million included £8.5 million of internally generated assets.

Impairment testing for CGUs containing goodwill
For the purposes of impairment testing, goodwill is allocated to the Group's CGUs as follows:

Group	2017 £m	2016 £m
Property Finance	**5.4**	5.4
Business Finance	**32.6**	32.6
Consumer Lending	**0.5**	0.5
At 31 December	**38.5**	38.5

No impairment losses were recognised in 2017 (2016: £nil) because the recoverable amounts of the CGUs were higher than their carrying values.

The recoverable amounts of the CGUs were calculated based on their value in use, determined by discounting the future cash flows (post-tax profits) to be generated from the continuing use of the CGU. Forecast cash flows were reduced by any earnings retained to support the growth in the underlying CGUs loan books through higher regulatory capital requirements. Forecast post-tax profits were based on expectations of future outcomes taking into account past experience and adjusted for anticipated revenue growth.

Intangible assets (continued)

The key assumptions used in the calculation of value in use were as follows:

	Post-tax	Pre-tax[1]
Post-tax discount rate:		
Property Finance	**12.0%**	**16.6%**
Business Finance	**12.5%**	**16.3%**
Consumer Lending	**13.0%**	**16.8%**
Cash flow period (Years)	**4**	**4**
Terminal value growth rate	**2.0%**	**2.0%**

[1] Management applies post-tax discount rates to post-tax cash flows when testing the CGU for impairment. The pre-tax discount rate is disclosed in accordance with IAS 36.

The post-tax discount rate is an estimate of the return that investors would require if they were to choose an investment that would generate cash flows of amount, timing and risk profile equivalent to those that the entity expects to derive from the asset. Subsequent to the Group's delisting from the stock exchange, calculation of the discount rate based on the capital asset pricing model used in 2016 was no longer appropriate. As such, the price-to-book ratio method was adopted as an alternative method incorporating target return on equity, growth rate and price-to-book ratio. The discount rate for each CGU was adjusted to reflect the risks inherent to the individual CGU.

Four years of cash flows were included in the discounted cash flow model based on a Board approved plan. A terminal value growth rate was than applied into perpetuity to extrapolate cash flows beyond the cash flow period. The terminal value growth rate was estimated by Management taking into account rates disclosed by comparable institutions. Sensitivity analysis on the cash flows identified that a decrease of the cash flows of 20% will not result in any impairment of the goodwill balance

The key assumptions described above may change in response to changes in economic and market conditions. However, the value in use of all CGUs was significantly greater than their carrying values and sensitivity analysis identified that an increase of 3.00% in each of the individual CGU discount rates will not result in any impairment of the goodwill balance.

17. Deferred tax

Accounting policy
Deferred tax is provided in full using the liability method on temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. The amount of deferred tax provided is based on the expected manner of realisation or settlement of the carrying amount of assets and liabilities, using tax rates enacted or substantively enacted at the statement of financial position reporting date. A deferred tax asset is recognised for unused tax losses, tax credits and deductible temporary differences to the extent that it is probable that future taxable profits will be available against which they can be utilised. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realised.

Deferred tax (continued)

Deferred tax assets are attributable as follows:

	2017	2016
	£m	£m
Accelerated tax depreciation	**13.6**	14.9
Share-based payments	**-**	1.1
Bad debt provision	**2.0**	1.8
Other	**0.1**	0.1
Deferred tax assets	**15.7**	17.9
At 1 January	**17.9**	14.1
Current period movement - recognised in income	**(0.4)**	1.8
Prior year adjustment	**(0.9)**	(0.2)
Share-based payments	**(1.1)**	0.9
Bad debt provision	**0.2**	1.3
At 31 December	**15.7**	17.9

The Group had a deferred tax asset of £15.7 million at 31 December 2017 (2016: £17.9 million) resulting primarily from decelerated capital allowances. The business plan projects profits in future years sufficient to recognise the £15.7 million deferred tax asset. The tax assets will unwind over the remaining life of the underlying leased assets with which they are associated.

A reduction in the UK corporation tax rate from 20% to 19% (effective from 1 April 2017) and further reductions to 17% (effective 1 April 2020) were substantively enacted on 16 March 2016. The deferred tax asset at 31 December 2017 has been calculated based on an aggregation of a rate of 18% substantively enacted at the statement of financial position reporting date and the additional 8% of tax suffered in relation to the banking surcharge that will unwind over the remaining life of the underlying assets with which they are associated.

18. Other assets

	Group 2017 £m	**Company 2017 £m**	Group & Company 2016 £m
Other debtors	**0.5**	**0.5**	1.9
Prepayments	**9.4**	**9.4**	14.2
Amounts due from group companies	**-**	**9.9**	-
Total other assets	**9.9**	**19.8**	16.1

19. Investment in subsidiaries

At 31 December 2017, the total investment in subsidiaries held at cost amounted to £102 (2016:£102).

20. Customer deposits

	2017	2016
	£m	£m
Instant access	**878.2**	636.6
Term deposits and notice accounts	**3,496.0**	3,301.9
Fair value adjustments for hedged risk	**2.0**	5.0
Total customer deposits	**4,376.2**	3,943.5

21. Amounts due to banks

Total amounts due to banks of £607.3 million at 31 December 2017 (2016: £147.7 million) includes £nil (2016: £24.8 million) which are monies arising from the sale and repurchase of Treasury Bills drawn under the Bank of England's Funding for Lending Scheme (FLS). Also included is £605.0 million (2016: £118.0 million) of deposits received from the Bank of England under the Term Funding Scheme (TFS) which fall due for repayment in 2020 and 2021. The TFS deposits are collateralised by loan assets of £902.2 million (2016: £160.8 million).

22. Provisions for liabilities and charges

	2017	2016
	£m	£m
At 1 January	**1.3**	0.9
Provisions utilised	**(0.6)**	(0.7)
Provisions made during the year	**2.1**	1.1
At 31 December	**2.8**	1.3

Financial Services Compensation Scheme
In common with all regulated UK deposit takers, the Group pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. The FSCS levy consists of two parts: a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes using the rights that have been assigned to it.

The FSCS meets these current claims by way of loans received from HM Treasury. The terms of these loans were interest only for the first three years, and the FSCS seeks to recover the interest cost, together with ongoing management expenses, via annual management levies on members, including the Group, over this period. The loan for the compensation levy has been repaid in full.

The Group's FSCS provision reflects market participation up to the reporting date. The above provision includes the estimated management expense levy for the scheme year 2016/17. This amount was calculated on the basis of the Group's current share of protected deposits taking into account the FSCS's estimate of total management expense levies for the scheme year.

Critical accounting estimates and judgements
Customer remediation and conduct issues
Provisions have been made in respect of various potential customer claims and represent management's best estimate of the likely costs. A provision of £2.5 million relates to potential instances of misrepresentation or breaches of contract by suppliers where the suppliers have become insolvent (and therefore the Group having limited recourse to those suppliers). The provision is calculated using management's estimate of complaints volumes, referral levels to the Financial Ombudsman Service (FOS), claim rates upheld internally and by FOS, redress payments and complaint handling costs.

23. Other liabilities

	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Other creditors	**46.2**	**10.7**	12.9	12.9
Accruals	**16.2**	**16.1**	14.2	14.1
Amounts due to group undertakings	**1.0**	**-**	1.7	1.7
Total other liabilities	**63.4**	**26.8**	28.8	28.7

Included in other creditors are amounts relating to sundry creditors, deferred incomes and other taxes.

Other creditors have increased to £46.2 million in 2017 (2016: £12.9 million). This is primarily due to amounts owing to a bank in relation to the purchase of a loan book.

24. Operating leases

Accounting policy
Operating lease income is recognised in the statement of profit and loss on a straight-line basis over the lease term unless a different systematic basis is more appropriate. Where an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor in compensation is charged to the statement of profit and loss in the period in which termination is made.

Leases as lessee
Non-cancellable operating lease rentals on land and buildings are payable as follows:

Leases as lessee	Group & Company 2017 £m	Group & Company 2016 £m
Less than 1 year	**2.0**	1.5
Between 1 and 5 years	**5.8**	3.4
More than 5 years	**1.8**	-
Total leases as lessee	**9.6**	4.9

Leases as lessor
Operating lease rentals receivable from agreements classified as property, plant and equipment, as disclosed in Note 16, are receivable as follows:

Leases as lessor	Group 2017 £m	Company 2017 £m	Group & Company 2016 £m
Less than 1 year	**8.6**	**8.6**	10.4
Between 1 and 5 years	**16.7**	**16.5**	16.0
More than 5 years	**1.5**	**1.5**	1.0
Total leases as lessor	**26.8**	**26.6**	27.4

25. Subordinated debt

Accounting policy
The subordinated debt is a non-derivative financial liability with fixed or determinable payments. The subordinated debt is recognised initially at fair value and subsequently measured at amortised cost. Interest costs arising are capitalised in accordance with agreed terms and incorporated into the total debt payable and recognised on an effective interest rate basis.

In 2015, the Shawbrook Bank Limited entered into a £75 million subordinated debt with its parent company, Shawbrook Group plc. The terms and conditions mirror the subordinated debt listed by the parent company on the London Stock Exchange on 28 October 2015.

	2017 £m	2016 £m
At 1 January	**76.1**	75.0
Interest expense	**6.4**	6.4
Repayment of interest	**(6.4)**	(5.3)
At 31 December	**76.1**	76.1

26. Share capital

Ordinary shares of £1.00 each: issued and fully paid

	2017 No.	2016 No.
Ordinary £1.00 shares	**175,487,207**	175,487,207

	2017 No.	**2017 £**	2016 No.	2016 £
On issue at 1 January and 31 December	**175,487,207**	**175,487,207**	175,487,207	175,487,207

Holders of these shares are entitled to dividends as declared from time to time and are entitled to one vote per share at general meetings of the Company. There are no restrictions on the rights implicit to the shares.

27. Capital securities

Accounting policy
In accordance with IAS 32 'Financial instruments: Presentation', the capital securities are classified as equity instruments based on the characteristics associated with its redemption and interest payments discussed fully below. No embedded derivative features were identified. Accordingly, the capital securities have been included in equity at the fair value of the proceeds received less any costs directly attributable to their issue, net of tax relief thereon. Any interest paid on the capital securities, net of tax relief thereon, is a distribution to holders of equity instruments and is recognised directly in equity on the payment date.

	2017 £m	2016 £m
Issue of capital securities	**125.0**	-

Capital securitiescontinued)

During the year the Shawbrook Group plc issued £125.0 million Fixed Rate Reset Perpetual Additional Tier 1 Write Down Capital Securities (the 'Securities') which was listed on the Irish Stock Exchange on 8 December 2017 and following the listing of the Securities to the market, Securities were issued from Shawbrook Bank Limited to Shawbrook Group plc on consistent terms as the listed Securities.

The Securities are perpetual securities in respect of which there is no fixed redemption date. The Securities may only be redeemed or repurchased by the Company for certain regulatory or tax reasons. Any optional redemption requires the prior consent of the Prudential Regulation Authority (PRA).

The Securities bear interest on their principal amount at an initial rate of 7.875% per annum until the first reset date of 8 December 2022. The reset rate of interest will be determined on the first reset date and on each fifth anniversary thereafter. Interest is payable on the Securities semi-annually in arrears commencing 8 June 2018 and is non-cumulative. Interest is fully discretionary and the Company may elect to cancel (in whole or in part) the interest otherwise scheduled to be paid.

There are a number of additional terms relating to events such as acquisition and wind up, however there are no circumstances in which the Group has an unavoidable obligation to issue a variable number of its own shares.

In the event of the Group's CET1 ratio falling below 7.00%, a 'Trigger Event', an 'Automatic Write Down' shall occur on the next business day, resulting in the irrevocable and automatic reduction of the full principal amount of Securities to zero and the cancellation of all accrued and unpaid interest and any other amounts arising under or in connection with the Securities.

28. Notes to the cash flow statement

Accounting policy
For the purposes of the statement of cash flows, cash and cash equivalents comprise cash and balances at central banks, loans and advances to banks and building societies and short-term highly liquid debt securities with less than three months to maturity from the date of acquisition. Loans to banks and building societies comprise cash balances and call deposits.

Non-cash items in the cash flow statement	Notes	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Capitalisation of subordinated debt interest	25	**6.4**	**6.4**	6.4	6.4
Depreciation	15	**13.2**	**13.2**	13.5	13.1
Amortisation of intangible assets	16	**4.0**	**4.0**	2.7	2.7
Provisions against loans and advances to customers	13	**23.3**	**23.2**	24.3	24.3
Amortisation of share scheme fair value	9	**7.5**	**7.5**	4.8	4.8
Total non-cash items		**54.4**	**54.3**	51.7	51.3

Cash and cash equivalents	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Cash and balances at central banks	**752.5**	**752.5**	429.9	429.9
Loans and advances to banks	**28.8**	**28.5**	24.1	24.1
Less: mandatory deposits with central banks	**(4.3)**	**(4.3)**	(4.0)	(4.0)
Cash and cash equivalents	**777.0**	**776.7**	450.0	450.0

Mandatory deposits are not available for use in the Group or Bank's day-to-day business and are non-interest bearing.

29. Financial instruments

Accounting policy
Financial assets and financial liabilities are recognised in the Group statement of financial position when the Group becomes a party to the contract provisions of the instrument.

Recognised financial assets and financial liabilities are initially measured at fair value. Transaction costs that are directly attributable to the acquisition or issue of financial assets and financial liabilities (other than financial assets and financial liabilities at fair value through profit or loss) are added to or deducted from the fair value of the financial assets or financial liabilities, as appropriate, on initial recognition. Transaction costs directly attributable to the financial asset or financial liabilities at fair value through profit or loss are recognised immediately in the statement of profit and loss.

If the transaction price differs from the fair value at initial recognition, the Group will account for such differences as follows:
> if fair value is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique that uses only data from observable markets, then the difference is recognised in the statement of profit and loss on initial recognition (i.e. day 1 profit or loss);
> in all other cases, the fair value will be adjusted to bring it in line with the transaction price (i.e. day 1 profit or loss will be deferred by including it in the initial carrying amount of the asset or liability).

After initial recognition, the deferred gain or loss will be released to the statement of profit and loss on a rational basis, only to the extent that it arises from a change in a factor (including time) that market participants would take into account when pricing the asset or liability.

Financial assets
All financial assets are recognised and derecognised on a trade date where the purchase or sale of a financial asset is under contract whose terms require delivery of the financial asset within the timeframe established by the market concerned, and are initially measured at fair value, plus transaction costs, except for those financial assets classified as fair value through profit or loss. Transaction costs directly attributable to the acquisition of financial assets classified as fair value through profit or loss are recognised immediately in the statement of profit and loss.

The Group classifies its financial assets in the following two categories:
> at fair value through profit or loss; and
> loan receivables.

Derivative financial instruments
The Group enters into a variety of derivative financial instruments some of which are held for trading while others are held to manage its exposure to interest rate risk and foreign exchange risk. Derivatives held include foreign exchange forward contracts, interest rate swaps and cross currency interest rate swaps. Further details of derivative financial instruments are disclosed in Note 14.

Derivatives are initially recognised at fair value at the date a derivative contract is entered into and are subsequently remeasured to their fair value at each statement of financial position reporting date. The resulting gain or loss is recognised in the statement of profit and loss immediately unless the derivative is designated and effective as a hedging instrument, in which event the timing of the recognition in the statement of profit and loss depends on the nature of the hedge relationship. A derivative with a positive fair value is recognised as a financial asset whereas a derivative with a negative fair value is recognised as a financial liability. A derivative is presented as a non-current asset or a non-current liability if the remaining maturity of the instrument is more than 12 months and it is not expected to be realised or settled within 12 months.

The Group has not classified any assets or liabilities as held to maturity or as available for sale.

Loan receivables
Loans and advances are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Loans and advances to banks and building societies are classified as loans and receivables. Loans and advances to customers include finance leases and instalment credit advances.

Subsequent to initial recognition, loans and receivables are measured at amortised cost using the effective interest method, less any impairment losses. In cases where there is a modification of a financial asset (i.e. the contractual terms governing the cash flows of the financial asset are renegotiated or modified), the Group assesses whether this modification results in derecognition. A modification results in derecognition when it gives rise to substantially different terms such as:

- Qualitative factors, such as contractual cash flows after modification are no longer payments of principal and interest, for example a change in the currency or change of counterparty, extensive change in interest rates, maturity, covenants. If these do not clearly indicate a substantial modification then;
- A quantitative assessment is performed to compare the present value of the remaining contractual cash flows under the original terms with the contractual cash flows under the revised terms discounted using the original effective interest rate. If the difference in present value is greater than 10% then the Group deems the arrangement is substantially different leading to derecognition.

The net investment in finance leases and instalment credit agreements represents the future lease rentals and instalments receivable less profit and costs allocated to future periods. Income is recognised throughout the life of the agreement to provide a constant rate of return on the net investment in each lease or instalment credit agreement.

Where an agreement is classified as an operating lease at inception, but is subsequently reclassified as a finance lease following a change to the agreement or an extension beyond the primary term, then the agreement is accounted for as a finance lease.

Financial liabilities

Customer deposits and amounts due to banks are non-derivative financial liabilities with fixed or determinable payments. Deposits and amounts due to banks are recognised initially at fair value and are subsequently measured at amortised cost using the effective interest method.

Derecognition of financial assets and liabilities

Derecognition is the point at which an asset or liability is removed from the statement of financial position. The Group's policy is to derecognise financial assets when the contractual rights to the cash flows from the financial asset have expired or when all the risks and rewards of ownership have been transferred.

The Group derecognises a financial liability when its contractual obligations are discharged, cancelled, or expired.

If the terms of the financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the net present value of the cash flows from the original financial asset is substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and the new financial asset is recognised at fair value.

The impairment loss before an unexpected restructuring is measured as follows:

- if the expected restructuring will not result in derecognition of the existing asset, then the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset; and
- if the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is then discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset.

Financial instruments (continued)

Fair value of financial assets and liabilities
The Group measures fair values in accordance with IFRS 13 'Fair Value Measurement', which defines fair value as 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. The Group also uses a fair value hierarchy that categorises into three levels the inputs to valuation techniques used to measure fair value which gives highest priority to quoted prices.

- **Level 1:** Quoted prices in active markets for identical assets or liabilities, for identical assets or liabilities that the entity can access at the measurement date;
- **Level 2:** Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices). A Level 2 input must be observable for substantially the full term of the instrument. Level 2 inputs include quoted prices for similar assets or liabilities in active markets, quoted prices for identical or similar assets or liabilities in markets that are not active, inputs other than quoted prices that are observable for the asset or liability, such as interest rates and yield curves observable at commonly quoted intervals, implied volatilities; and credit spreads. Assets and liabilities classified as Level 2 have been valued using models whose inputs are observable in an active market; and
- **Level 3:** Inputs for the asset or liabilities that are not based on observable market data (unobservable inputs).

Fair values of financial assets and financial liabilities that are traded in active markets are based on quoted market prices or dealer price quotations. The Group holds financial assets and liabilities for which quoted prices are not available, such as over the counter (OTC) derivatives (interest rate swaps, options and foreign currency derivatives). For these financial instruments, the Group uses valuation techniques to estimate fair value. The valuation techniques used include discounted cash flow models and Black-Scholes option pricing. These valuation techniques use as their basis independently sourced market parameters, such as interest rate yield curves, option volatilities and currency rates.

The Group uses generally accepted valuation models to determine the fair value of simple and liquid financial instruments, such as interest rate and currency swaps, which involve minimum judgement. The use of observable market prices and model inputs when available reduces the need for Management judgement and estimation, as well as the uncertainty related with the estimated fair value. The available of observable market prices and inputs varies depending on the products and markets and is prone to changes based on general conditions and specific events in the financial markets.

The consideration of factors such as the scale and frequency of trading activity, the availability of prices and the size of bid/offer spreads assists in the assessment of whether a market is active. If, in the opinion of Management, a significant proportion of an instrument's carrying amount is driven by unobservable inputs, the instrument in its entirety is classified as valued at Level 3 of the fair value hierarchy. 'Level 3' in this context means that there is little or no current market data available from which to determine the level at which an arm's length transaction would be likely to occur. It generally does not mean that there is no market data available at all upon which to base a determination of fair value (consensus pricing data may, for example, be used).

The Group does not adjust fair value estimates derived from models for any factors such as credit risk, liquidity risk or model uncertainties. For measuring derivatives that might change classification from being an asset to a liability or vice versa fair values do not take into consideration either the credit valuation adjustment or the debit valuation adjustment as it is deemed to be immaterial.

Cash and balances at central banks
Fair value approximates to carrying value as cash and balances at central banks have minimal credit losses and are either short-term in nature or re-price frequently.

Loans and advances to banks, customer deposits, amounts due to banks and derivatives
Fair value is estimated by using discounted cash flows applying either market rates where practicable or rates offered with similar characteristics by other financial institutions. The fair value of floating rate placements, fixed rate placements with less than six months to maturity and overnight deposits is considered to approximate to their carrying amount.

Fair values of derivatives are obtained from quoted market prices in active markets and, where these are not available, from valuation techniques including discounted cash flows.

Financial instruments (continued)

Loans and advances to customers
Fair value is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the statement of financial position reporting date, and adjusted for future credit losses if considered material.

Subordinated debt
Fair values are based on quoted prices where available or by discounting cash flows using market rates.

Fair value hierarchy
The table below analyses the Group's financial instruments measured at amortised cost into a fair value hierarchy:

	2017 Level 3 £m	**2017 Level 2 £m**	**2017 Level 1 £m**	2016 Level 3 £m	2016 Level 2 £m	2016 Level 1 £m
Financial assets						
Cash and balances at central banks	-	-	**752.5**	-	-	429.9
Loans and advances to banks	-	**28.8**	-	-	24.1	-
Loans and advances to customers	**4,844.3**	-	-	4,050.4	-	-
Financial liabilities						
Customer deposits	-	**4,376.2**	-	-	3,943.5	-
Amounts due to banks	-	**607.3**	-	-	147.7	-
Subordinated debt liability	-	**76.1**	-	-	76.1	-

There were no transfers of assets or liabilities between the levels of the fair value hierarchy during the year (2016: £nil).

The table below analyses the Group's financial instruments measured at fair value into a fair value hierarchy:

	2017 Level 3 £m	**2017 Level 2 £m**	**2017 Level 1 £m**	2016 Level 3 £m	2016 Level 2 £m	2016 Level 1 £m
Financial assets						
Derivative financial instruments	-	**1.8**	-	-	5.2	-
Financial liabilities						
Derivative financial instruments	-	**(3.4)**	-	-	(0.4)	-

Financial instruments (continued)

The fair values of all financial assets and financial liabilities by class together with their carrying amounts shown in the statement of financial position are shown in the following table:

	Loans and receivables £m	Other liabilities at amortised cost £m	Total carrying amount £m	Fair value £m
At 31 December 2017				
Cash and balances at central banks	**752.5**	-	**752.5**	**752.5**
Loans and advances to banks	**28.8**	-	**28.8**	**28.8**
Loans and advances to customers	**4,844.3**	-	**4,844.3**	**5,045.9**
	5,625.6	-	**5,625.6**	**5,827.2**
Customer deposits	-	**4,376.2**	**4,376.2**	**4,369.3**
Amounts due to banks	-	**607.3**	**607.3**	**594.5**
Subordinated debt liability	-	**76.1**	**76.1**	**81.0**
	-	**5,059.6**	**5,059.6**	**5,044.8**
At 31 December 2016				
Cash and balances at central banks	429.9	-	429.9	429.9
Loans and advances to banks	24.1	-	24.1	24.1
Loans and advances to customers	4,050.4	-	4,050.4	4,100.5
	4,504.4	-	4,504.4	4,554.5
Customer deposits	-	3,943.5	3,943.5	3,963.8
Amounts due to banks	-	147.7	147.7	147.7
Subordinated debt liability	-	76.1	76.1	76.0
	-	4,167.3	4,167.3	4,187.5

30. Risk management

The main areas of risk that the business is exposed to are:
credit risk (see 30.1);
liquidity risk (see 30.2);
market risk (see 30.3);
capital risk and management (see 30.4);
operational risk; and
conduct risk.

30.1 Credit risk
Credit risk is the risk of suffering financial loss should borrowers or counterparties default on their contractual obligations to the Group. These risks are managed by the Board Risk Committee and the Asset and Liability Committee. This risk has two main components:
customer risk (individual and business lending) (see 30.1.1); and
treasury risk (see 30.1.2).

Risk management (continued)

The Group's maximum exposure to credit risk is the carrying value of its financial assets, without taking account of any underlying collateral, and contractual commitments, which represent agreements entered into but not advanced as at 31 December 2017.

	2017 £m	2016 £m
Assets		
Cash and balances at central banks	**752.5**	429.9
Loans and advances to banks	**28.8**	24.1
Loans and advances to customers	**4,844.3**	4,050.4
Derivative financial assets	**1.8**	5.2
	5,627.4	4,509.6
Contractual commitments	**623.0**	459.2
Maximum exposure to credit risk	**6,250.4**	4,968.8

The contractual commitments are a combination of loan commitments and committed undrawn facilities.

The amount of collateral held at 31 December 2017 is £4,250.9 million (2016: £3,603.0 million) of which £3,197.8 million (2016: £2,524.3 million) is in the form of residential and commercial property and £1,053.1 million (2016: £1,078.7 million) is secured on other assets and debt receivables. Collateral held in relation to secured loans is capped at the amount outstanding on an individual loan basis.

Credit quality of assets
Loans and receivables
During the year the Group developed and implemented a credit grading scorecard. The credit scoring scale is used to determine an individual internal credit score based on the point-in-time PDs of the individual agreements. The point-in-time PD is an internal parameter used within the Group's Advanced Internal Risk Based capital models which aims to estimate the probability of default over the next 12 months based on account characteristics and customer behavioural data. Exposures are categorised as follows:
> **Low Risk:** where assets are not past due and have a point-in-time PD less than or equal to 0.38%;
> **Medium Risk:** where assets are not past due and have a point-in-time PD greater than 0.38% and less than or equal to 1.76%;
> **High Risk:** where assets are not past due and have a point-in-time PD of greater than 1.76%.

The credit grading scorecard cannot retrospectively be applied to the FY 2016 results, and therefore the FY 2017 results are not directly comparable to the FY 2016 results.

Risk management (continued)

The credit quality of assets that are neither past due nor impaired are as follows:

	Property Finance		Business Finance		Consumer Lending		Total	
At 31 December 2017	**£m**	**%**	**£m**	**%**	**£m**	**%**	**£m**	**%**
Low Risk	**1,700.7**	**54.6**	**119.9**	**11.8**	**125.3**	**20.5**	**1,945.9**	**41.0**
Medium Risk	**1,270.8**	**40.8**	**421.5**	**41.5**	**411.4**	**67.3**	**2,103.7**	**44.4**
Higher Risk	**143.3**	**4.6**	**474.3**	**46.7**	**74.6**	**12.2**	**692.2**	**14.6**
Total neither past due nor impaired	**3,114.8**	**100.0**	**1,015.7**	**100.0**	**611.3**	**100.0**	**4,741.8**	**100.0**

In 2016 the Group defined three classifications of credit quality (low risk, medium risk and higher risk) for all credit exposures. These were based on the following criteria:

Property Finance: For the residential mortgage portfolio, a risk rating scale is applied to the individual loans and weighs the propensity of non-performance and write-offs. The provisioning methodology within the residential portfolio was amended during the year to utilise credit scoring to drive loan level probability of defaults. The combined propensity scores are scaled into low risk, medium risk and higher risk. In the Commercial Mortgages portfolio loans are classified as low risk, medium risk and higher risk on a case by case basis based on the circumstances of every case.

Business Finance: Loans are classified as low risk, medium risk and higher risk on a case by case basis. Classification is based on Management's review of the individual circumstances of every case.

Consumer Lending: Any loans that are 90 days or more past due are deemed to be impaired. Loans that are neither past due nor impaired are considered by Management to be low risk.

	Property Finance		Business Finance		Consumer Lending		Total	
At 31 December 2016	£m	%	£m	%	£m	%	£m	%
Low Risk	2,397.5	98.1	986.5	95.1	460.8	100.0	3,844.8	97.5
Medium Risk	38.5	1.6	50.3	4.9	-	-	88.8	2.3
Higher Risk	7.9	0.3	0.1	-	-	-	8.0	0.2
Total neither past due nor impaired	2,443.9	100.0	1,036.9	100.0	460.8	100.0	3,941.6	100.0

30.1.1 Customer risk

The Group maintains a forbearance policy for the servicing and management of customers who are in financial difficulty and require some form of concession to be granted, even if this concession entails a loss for the Group. A concession may be either of the following:

a modification of the previous terms and conditions of an agreement, which the borrower is considered unable to comply with due to its financial difficulties, to allow for sufficient debt service ability, that would not have been granted had the borrower not been in financial difficulties; or

a total or partial refinancing of an agreement that would not have been granted had the borrower not been in financial difficulties.

Forbearance in relation to an exposure can be temporary or permanent depending on the circumstances, progress on financial rehabilitation and the detail of the concession(s) agreed. A forbearance classification can be discontinued when all of the following conditions have been met:

the exposure is considered as performing, including, if it has been reclassified from the non-performing category, after an analysis of the financial condition of the borrower shows it no longer meets the conditions to be considered as non-performing;

regular payments of more than an insignificant aggregate amount of principal or interest have been made during at least half of the probation period; and

none of the exposures to the debtor is more than 30 days past due at the end of the probation period.

Risk management (continued)

Details of the forbearance arrangements in place are set out in the tables below:

Forbearance at 31 December 2017	**Number**	**Capital balances £m**	**Provisions £m**	**Coverage %**
Property Finance	**239**	**16.2**	**1.0**	**6.2%**
Business Finance	**361**	**35.8**	**5.3**	**14.8%**
Consumer Lending	**830**	**5.3**	**2.8**	**52.8%**
Total	**1,430**	**57.3**	**9.1**	**15.9%**

Forbearance at 31 December 2016	Number	Capital balances £m	Provisions £m	Coverage %
Property Finance	191	13.6	0.7	5.1%
Business Finance	237	30.1	3.3	11.0%
Consumer Lending	273	1.8	0.6	33.3%
Total	701	45.5	4.6	10.1%

There were seven property repossessions during the year (2016: six). The total carrying value of these assets was £1.1 million (2016: £2.1 million). Of the seven repossessions, four were disposed of by 31 December 2017 and the remaining three are currently on the market.

Loans and advances to customers are reviewed regularly to determine whether there is any objective evidence of impairment and assets are categorised as detailed in the tables below:

Type of impairment assessment	**Description**
Individual impairment	Where specific circumstances indicate that a loss is likely to be incurred.
Collective impairment	Impairment allowances are calculated for each portfolio on a collective basis, given the homogenous nature of the assets in the portfolio.

Risk categorisation	**Description**
Neither past due nor impaired	Loans that are not in arrears and which do not meet the impaired asset definition. This segment can include assets subject to forbearance solutions.
Past due but not impaired	Loans past due but not impaired consist predominantly of loans in Property Finance and Business Finance that are past due and individually assessed as not being impaired. This definition also includes unsecured loans in the Consumer Lending division that are past due but not more than 90 days.
Impaired assets	Loans that are in arrears or where there is objective evidence of impairment and where the carrying amount of the loan exceeds the expected recoverable amount. This definition also includes unsecured loans in the Consumer Lending division that are more than 90 days in arrears and carry identified impairment.

The Group enters into agreements with customers and where appropriate takes security. Loan receivables include amounts secured against property (commercial and residential), or against other assets such as asset backed loans and invoice receivables. Finance lease and instalment credit is secured on a variety of assets including, but not limited to, plant and machinery.

Risk management (continued)

The Group profile of the loan receivable book is shown below:

	2017 £m	2016 £m
Loan receivables	**4,418.7**	3,639.5
Finance lease receivables	**79.8**	93.6
Instalment credit receivables	**348.0**	316.9
Fair value adjustments for hedged risk	**(2.2)**	0.4
Total loans and advances to customers	**4,844.3**	4,050.4

Loan receivables	2017 £m	2016 £m
Neither past due nor impaired	**4,329.4**	3,548.7
Past due but not impaired:		
Up to 30 days	**12.8**	18.3
30-60 days	**40.1**	40.2
60-90 days	**10.4**	15.5
Over 90 days	**18.4**	15.8
Total past due but not impaired	**81.7**	89.8
Impaired assets	**27.3**	14.6
	4,438.4	3,653.1
Less: allowances for impairment losses	**(19.7)**	(13.6)
Net loan receivables	**4,418.7**	3,639.5
Fair value adjustments for hedged risk	**(2.2)**	0.4
	4,416.5	3,639.9

The Group enters into agreements with customers and where appropriate takes security. The security for loans to customers is in the form of a first or second charge over property and debt receivables. Finance leases and instalment credit are secured on the underlying assets which can be repossessed in the event of a default. The Group security profile of loans and advances to customers is shown below:

	2017 £m	2016 £m
Secured on commercial and residential property	**3,197.6**	2,524.3
Secured on debt receivables	**456.6**	545.4
Secured by finance lease and instalment credit assets	**439.7**	421.3
Secured on other assets	**68.3**	49.3
Total secured receivables	**4,162.2**	3,540.3
Unsecured	**715.9**	534.5
Gross loans and advances to customers	**4,878.1**	4,074.8

Risk management (continued)

Collateral held in relation to secured loans is capped, after taking into account the first charge balance, at the amount outstanding on an individual loan basis.

Finance lease receivables	2017 £m	2016 £m
Neither past due nor impaired	**72.0**	82.3
Past due but not impaired:		
Up to 30 days	**2.9**	4.6
30-60 days	**1.9**	1.1
60-90 days	**0.9**	0.4
Over 90 days	**0.9**	2.3
Total past due but not impaired	**6.6**	8.4
Impaired assets	**10.3**	11.4
	88.9	102.1
Less: allowances for impairment losses	**(9.1)**	(8.5)
Net finance lease receivables	**79.8**	93.6

Instalment credit receivables	2017 £m	2016 £m
Neither past due nor impaired	**340.4**	310.6
Past due but not impaired:		
Up to 30 days	**4.9**	3.6
30-60 days	**2.2**	0.9
60-90 days	**0.3**	0.6
Over 90 days	**0.9**	1.3
Total past due but not impaired	**8.3**	6.4
Impaired assets	**2.1**	2.2
	350.8	319.2
Less: allowances for impairment losses	**(2.8)**	(2.3)
Net instalment credit receivables	**348.0**	316.9

Risk management (continued)

31 December 2017	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
Neither past due nor impaired	**3,114.8**	**1,015.7**	**611.3**	**4,741.8**
Past due but not impaired:				
Up to 30 days	**9.2**	**10.4**	**1.0**	**20.6**
30-60 days	**32.8**	**4.0**	**7.4**	**44.2**
60-90 days	**7.8**	**1.2**	**2.6**	**11.6**
Over 90 days	**18.1**	**2.1**	**-**	**20.2**
Total past due but not impaired	**67.9**	**17.7**	**11.0**	**96.6**
Impaired assets	**13.3**	**21.5**	**4.9**	**39.7**
	3,196.0	**1,054.9**	**627.2**	**4,878.1**
Fair value adjustments for hedged risk	**(2.7)**	**-**	**0.5**	**(2.2)**
Less: allowances for impairment losses	**(6.3)**	**(15.0)**	**(10.3)**	**(31.6)**
Net loans and advances to customers	**3,187.0**	**1,039.9**	**617.4**	**4,844.3**

31 December 2016	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
Neither past due nor impaired	2,443.9	1,036.9	460.8	3,941.6
Past due but not impaired:				
Up to 30 days	13.8	12.0	0.7	26.5
30-60 days	33.6	4.3	4.3	42.2
60-90 days	10.7	4.2	1.6	16.5
Over 90 days	12.2	7.2	-	19.4
Total past due but not impaired	70.3	27.7	6.6	104.6
Impaired assets	10.1	14.1	4.0	28.2
	2,524.3	1,078.7	471.4	4,074.4
Fair value adjustments for hedged risk	-	-	0.4	0.4
Less: allowances for impairment losses	(5.2)	(12.4)	(6.8)	(24.4)
Net loans and advances to customers	2,519.1	1,066.3	465.0	4,050.4

Risk management (continued)

The Group's lending portfolio is geographically diversified across the UK as shown below:

31 December 2017	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
East Anglia	**99.0**	**75.3**	**25.6**	**199.9**
East Midlands	**100.5**	**34.7**	**48.6**	**183.8**
Greater London	**1,233.8**	**169.8**	**64.9**	**1,468.5**
Guernsey/Jersey/Isle of Man	**18.6**	**47.0**	**0.1**	**65.7**
North East	**45.5**	**16.4**	**29.9**	**91.8**
North West	**264.5**	**159.9**	**75.4**	**499.8**
Northern Ireland	**13.6**	**2.8**	**1.7**	**18.1**
Scotland	**183.0**	**71.0**	**76.9**	**330.9**
South East	**648.3**	**169.3**	**109.9**	**927.5**
South West	**239.5**	**89.7**	**48.3**	**377.5**
Wales	**69.4**	**84.8**	**24.4**	**178.6**
West Midlands	**125.0**	**74.8**	**62.0**	**261.8**
Yorkshire/Humberside	**155.3**	**59.4**	**59.5**	**274.2**
Gross loans and advances to customers	**3,196.0**	**1,054.9**	**627.2**	**4,878.1**

31 December 2016	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
East Anglia	84.3	71.1	21.1	176.5
East Midlands	75.2	26.9	36.8	138.9
Greater London	911.6	214.7	48.3	1,174.6
Guernsey/Jersey/Isle of Man	6.1	0.6	0.1	6.8
North East	38.5	11.3	23.7	73.5
North West	221.0	151.8	55.9	428.7
Northern Ireland	10.6	3.7	0.8	15.1
Scotland	157.5	96.9	60.9	315.3
South East	539.8	191.6	80.1	811.5
South West	198.3	107.5	36.8	342.6
Wales	57.1	70.1	17.9	145.1
West Midlands	104.1	64.1	47.2	215.4
Yorkshire/Humberside	120.2	68.4	41.8	230.4
Gross loans and advances to customers	2,524.3	1,078.7	471.4	4,074.4

Risk management (continued)

The Group's lending portfolio falls into the following concentrations by loan size:

31 December 2017	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
0 - £50k	**246.1**	**164.6**	**627.0**	**1,037.7**
£50k - £100k	**369.2**	**79.7**	**0.2**	**449.1**
£100k - £250k	**784.9**	**113.3**	**-**	**898.2**
£250k - £500k	**657.0**	**80.3**	**-**	**737.3**
£500k - £1 million	**478.1**	**106.1**	**-**	**584.2**
£1 million - £2.5 million	**379.2**	**153.7**	**-**	**532.9**
£2.5 million - £5 million	**167.1**	**80.2**	**-**	**247.3**
£5 million - £10 million	**61.8**	**77.4**	**-**	**139.2**
£10 million - £25 million	**52.6**	**199.6**	**-**	**252.2**
Gross loans and advances to customers	**3,196.0**	**1,054.9**	**627.2**	**4,878.1**

31 December 2016	Property Finance £m	Business Finance £m	Consumer Lending £m	Total £m
0 - £50k	249.6	170.3	471.3	891.2
£50k - £100k	312.6	80.2	0.1	392.9
£100k - £250k	622.5	106.3	-	728.8
£250k - £500k	495.8	93.2	-	589.0
£500k - £1 million	371.8	100.0	-	471.8
£1 million - £2.5 million	283.2	118.6	-	401.8
£2.5 million - £5 million	110.1	81.2	-	191.3
£5 million - £10 million	67.2	91.2	-	158.4
£10 million - £25 million	11.5	237.7	-	249.2
Gross loans and advances to customers	2,524.3	1,078.7	471.4	4,074.4

30.1.2 Treasury risk

Treasury risk arises from the wholesale investments made by the Group's Treasury function, which is responsible for managing this aspect of credit risk in line with the Board approved risk appetite and wholesale credit policies. The Group's credit quality of loans and advances to banks is assessed by rating agency designation as at 31 December 2017, based on Moody's long-term ratings.

Loans and advances to banks	2017 £m	2016 £m
Aa3	**12.2**	-
A1	**2.5**	15.6
A2	**-**	1.1
A3	**14.1**	7.4
Total credit risk	**28.8**	24.1

The Group only lends to UK high street banks. Deposits are placed either overnight or for a short-term with a duration of less than three months. No collateral or other credit enhancements are held against loans and advances to banks.

Risk management (continued)

The Group's exposure to the Bank of England is set out below:

Loans and advances to central banks	2017 £m	2016 £m
Aa1	-	429.9
Aa2	**752.5**	-

Credit risk derived from derivative transactions is mitigated by collateralising the exposures. Such collateral is subject to the standard industry CSA and is paid or received on a regular basis. At 31 December 2017, cash collateral of £3.9 million had been received by the Group (2016: £4.8 million).

30.2 Liquidity risk

Accounting policy
Liquidity risk is the risk that the Group is unable to meet its current and future financial obligations as they fall due, or is only able to do so at excessive cost.

The Group has, therefore, developed comprehensive funding and liquidity policies to ensure that it maintains sufficient liquid assets to be able to meet all its financial obligations and maintain public confidence.

The Group's Treasury function is responsible for the day-to-day management of the Group's liquidity and wholesale funding. The Board sets limits over the level, composition, and maturity of liquidity and deposit funding balances, reviewing these at least annually. Compliance with these limits is monitored daily by Finance and Risk function personnel independent of the Treasury function. Additionally, a combined liquidity stress test is performed daily and a series of other liquidity stress tests are performed monthly by the Risk function and formally reported to ALCo and the Board to ensure that the Group maintains adequate liquidity for business purposes even under stressed conditions.

The Group reports its liquidity position against its liquidity coverage ratio, net stable funding ratio and other key regulatory ratios for regulatory purposes

Funding for Lending Scheme (FLS)
The Group is a participant in the FLS which enables it to borrow highly liquid UK Treasury bills in exchange for eligible collateral. The Treasury bills issued are for an original maturity of nine months and if delivered back prior to their maturity date can be exchanged for further nine-month bills. Costs of borrowing are charged directly to the statement of profit and loss.

The Treasury bills are not recorded on the Group's statement of financial position as ownership remains with the Bank of England. The risks and rewards of the collateral provided remains with the Group and continue to be recognised in the Group's financial statements.

Term Funding Scheme (TFS)
The Term Funding Scheme (TFS) was announced by the Bank of England on 4 August 2016 and became effective from 19 September 2016. The TFS is designed to reinforce the transmission of reductions in the Bank of England's official interest rate (Bank Rate) to those interest rates actually faced by households and businesses by providing term funding to banks at rates close to Bank Rate. It is a monetary policy tool of the Monetary Policy Committee and will be operated as part of the Asset Purchase Facility.

The TFS allows participants to borrow central bank reserves in exchange for eligible collateral. The Group had drawn £605.0 million as at 31 December 2017 (2016: £118.0 million). This is included within 'Amounts due to banks' on the statement of financial position as detailed in Note 21.

Risk management (continued)

The table below analyses the Group's contractual undiscounted cash flows of its financial assets and liabilities:

At 31 December 2017	Carrying amount £m	Gross nominal inflow/ (outflow) £m	Less than 1 month £m	1-3 months £m	3 months to 1 year £m	1-2 years £m	2-5 years £m	More than 5 years £m
Assets								
Cash and balances at central banks	**752.5**	**752.5**	**748.2**	**-**	**-**	**-**	**-**	**4.3**
Loans and advances to banks	**28.8**	**28.8**	**28.8**	**-**	**-**	**-**	**-**	**-**
Loans and advances to customers	**4,844.3**	**4,989.8**	**211.8**	**218.7**	**646.3**	**690.8**	**1,222.7**	**1,999.5**
	5,625.6	**5,771.1**	**988.8**	**218.7**	**646.3**	**690.8**	**1,222.7**	**2,003.8**
Liabilities								
Customer deposits	**(4,376.2)**	**(4,448.7)**	**(1,026.3)**	**(317.1)**	**(1,818.7)**	**(837.3)**	**(440.1)**	**(9.2)**
Amounts due to banks	**(607.3)**	**(612.4)**	**(2.4)**	**-**	**-**	**-**	**(610.0)**	**-**
Subordinated debt liability	**(76.1)**	**(127.1)**	**-**	**-**	**(7.5)**	**(6.4)**	**(19.1)**	**(94.1)**
	(5,059.6)	**(5,188.2)**	**(1,028.7)**	**(317.1)**	**(1,826.2)**	**(843.7)**	**(1,069.2)**	**(103.3)**

At 31 December 2016	Carrying amount £m	Gross nominal inflow/ (outflow) £m	Less than 1 month £m	1-3 months £m	3 months to 1 year £m	1-2 years £m	2-5 years £m	More than 5 years £m
Assets								
Cash and balances at central banks	429.9	429.9	425.9	-	-	-	-	4.0
Loans and advances to banks	24.1	24.1	24.1	-	-	-	-	-
Loans and advances to customers	4,050.4	4,174.9	115.4	137.6	561.0	649.9	1,213.3	1,497.7
	4,504.4	4,628.9	565.4	137.6	561.0	649.9	1,213.3	1,501.7
Liabilities								
Customer deposits	(3,943.5)	(3,887.9)	(791.9)	(250.3)	(1,705.4)	(634.1)	(506.2)	-
Amounts due to banks	(147.7)	(148.9)	(5.3)	(0.1)	(24.6)	(0.3)	(118.6)	-
Subordinated debt liability	(76.1)	(133.5)	-	-	(7.5)	(6.4)	(19.1)	(100.5)
	(4,167.3)	(4,170.3)	(797.2)	(250.4)	(1,737.5)	(640.8)	(643.9)	(100.5)

Risk management (continued)

The following table sets out the components of the Group's liquidity reserve:

	2017 Carrying amount £m	2016 Carrying amount £m
Cash and balances at central banks	**752.5**	429.9
Less: mandatory deposits with central banks	**(4.3)**	(4.0)
Loans and advances to banks	**28.8**	24.1
Debt securities	**100.9**	213.8
Total liquidity reserve	**877.9**	663.8

The total liquidity reserve includes £100.9 million (2016: £213.8 million) of securities issued by the Bank of England through FLS participation which are not recognised on the statement of financial position.

The average liquidity reserve throughout the year was £708.4 million (2016: £745.1 million).

Asset encumbrance
The Group's assets can be used to support collateral requirements for central bank operations or third party repurchase transactions. Assets that have been set aside for such purposes are classified as 'encumbered assets' and cannot be used for other purposes.

All other assets are defined as 'unencumbered assets'. These comprise assets that are readily available to secure funding or meet collateral requirements, and assets that are not subject to any restrictions but are not readily available for use.

The table below sets out the availability of the Group's assets to support future funding:

Asset encumbrance 2017	**Encumbered (pledged as collateral) £m**	**Unencumbered (available as collateral) £m**	**Unencumbered other £m**	**Total £m**
Cash and balances at central banks	**4.3**	**-**	**748.2**	**752.5**
Loans and advances to banks	**-**	**28.8**	**-**	**28.8**
Loans and advances to customers	**1081.7**	**3,762.6**	**-**	**4,844.3**
Derivative financial assets	**-**	**-**	**1.8**	**1.8**
Property, plant and equipment	**-**	**36.1**	**3.5**	**39.6**
Non-financial assets	**-**	**-**	**85.0**	**85.0**
Total assets	**1,086.0**	**3,827.5**	**838.5**	**5,752.0**

Asset encumbrance 2016	Encumbered (pledged as collateral) £m	Unencumbered (available as collateral) £m	Unencumbered other £m	Total £m
Cash and balances at central banks	4.0	-	425.9	429.9
Loans and advances to banks	-	24.1	-	24.1
Loans and advances to customers	695.2	3,355.2	-	4,050.4
Derivative financial assets	-	-	5.2	5.2
Property, plant and equipment	-	38.1	4.5	42.6
Non-financial assets	-	-	87.6	87.6
Total assets	699.2	3,417.4	523.2	4,639.8

Risk management (continued)

Liquidity risk – stress testing
Stress testing is a major component of liquidity risk management and the Group has developed a range of scenarios covering a range of market wide and firm specific factors. A comprehensive stress testing exercise is conducted at least annually and the methodology is incorporated into the Group's statement of financial position risk management model to ensure that stress tests are run on a regular basis. The output of stress testing is circulated to the Board and to the Asset and Liability Committee (ALCo) who use the results to decide whether to amend the Group's risk appetite and liquidity limits.

30.3 Market risk
Market risk is the risk that the value of, or income arising from, the Group's assets and liabilities change as a result of changes in market prices, the principal element being interest rate risk.

The Group's objective is to manage and control market risk exposures while maintaining a market profile consistent with the Group's risk appetite.

The Group's Treasury function is responsible for managing the Group's exposure to all aspects of market risk within the operational limits set out in the Group's treasury policies. The ALCo approves the Group's treasury policies and receives regular reports on all aspects of market risk exposure, including interest rate risk.

The Group has minimal foreign currency exposure and does not engage in any treasury trading operations.

Interest rate risk
Interest rate risk is the risk of loss arising from adverse movements in market interest rates. Interest rate risk arises from the loan and savings products that the Group offers. This risk is managed through the use of appropriate financial instruments, including derivatives, with established risk limits, reporting lines, mandates and other control procedures.

Basis risk
Basis risk is the risk of loss arising from changes in the relationship between interest rates which have similar but not identical characteristics (for example, LIBOR and the Bank of England base rate). This is monitored closely and regularly reported to the ALCo. This risk is managed by matching and where appropriate and necessary, through the use of derivatives, with established risk limits and other control procedures.

The Group's forecasts and plans take account of the risk of interest rate changes and are prepared and stressed accordingly, in line with PRA guidance.

Foreign exchange risk
Foreign exchange risk is the risk that the value of, or net income arising from, assets and liabilities changes as a result of movements in exchange rates. The Group has low levels of foreign exchange risk which is managed by natural hedging and appropriate financial instruments including derivatives. The table below sets out the Group's exposure to foreign exchange risk:

Assets and liabilities in foreign currencies at Sterling carrying values 2017	**Euros £m**	**US Dollars £m**	**Australian Dollars £m**
Loans and advances to banks	**1.9**	**(0.8)**	**(0.1)**
Loans and advances to customers	**24.4**	**7.7**	**0.1**
Net position	**26.3**	**6.9**	**-**

Assets and liabilities in foreign currencies at Sterling carrying values 2016	Euros £m	US Dollars £m	Australian Dollars £m
Loans and advances to banks	0.4	(0.9)	-
Loans and advances to customers	12.9	6.6	-
Net position	13.3	5.7	-

Risk management (continued)

Foreign exchange sensitivity
The Group estimates that a 5% movement in exchange rates would have no greater impact on the 2017 profit than an increase or decrease of £1.7 million.

Interest rate sensitivity gap
The Group considers a parallel 200 basis points (bps) movement to be appropriate for scenario testing given the current economic outlook and industry expectations. The Group estimates that a +/- 200 bps movement in interest rates paid/received would have impacted the economic value of equity as follows:
+200 bps – £10.5 million negative (2016: £9.5 million positive)
-200 bps – £41.0 million positive (2016: £12.1 million positive)

In addition, the effect of the same two interest rate shocks are applied to the statement of financial position at year end, to determine how net interest income may change on an annualised basis for one year, as follows:
+200 bps – £20.8 million positive (2016: £20.0 million positive)
-200 bps – £4.0 million positive (2016: £1.9 million positive)

In preparing the sensitivity analyses above, the Group makes certain assumptions consistent with expected and contractual re-pricing behaviour as well as behavioural repayment profiles, under the two interest scenarios, of the underlying statement of financial position items. The results also include the impact of hedge transactions.

The following table summarises the re-pricing periods for the Group's assets and liabilities at 31 December 2017. Items are allocated to time bands by reference to the earlier of the next contractual interest rate change and the maturity date.

31 December 2017	Within 3 months £m	3 months but less than 6 months £m	6 months but less than 1 year £m	1 year but less than 5 years £m	More than 5 years £m	Non-interest bearing £m	Total £m
Assets							
Cash and balances at central banks	748.2	-	-	-	-	4.3	752.5
Loans and advances to banks	28.8	-	-	-	-	-	28.8
Loans and advances to customers	2,495.5	210.1	363.6	1,533.5	296.4	(54.8)	4,844.3
Derivative financial assets	-	-	-	-	-	1.8	1.8
Other non-financial assets	3.6	2.1	4.1	22.2	4.8	87.8	124.6
	3,276.1	212.2	367.7	1,555.7	301.2	39.1	5,752.0
Liabilities							
Customer deposits	1,412.4	787.7	955.6	1,212.6	7.9	-	4,376.2
Amounts due to banks	607.3	-	-	-	-	-	607.3
Derivative financial liabilities	-	-	-	-	-	3.4	3.4
Other non-financial liabilities	-	-	-	-	-	74.0	74.0
Subordinated debt liability	-	-	-	-	76.1	-	76.1
Total equity	-	-	-	-	-	615.0	615.0
	2,019.7	787.7	955.6	1,212.6	84.0	692.4	5,752.0
Notional values of derivatives	578.0	(25.0)	(282.0)	(240.0)	(31.0)	-	-
Interest rate sensitivity gap	1,834.4	(600.5)	(869.9)	103.1	186.2	(653.3)	-
Cumulative gap	1,834.4	1,233.9	364.0	467.1	653.3	-	-

Risk management (continued)

The following table summarises the re-pricing periods for the Group's assets and liabilities at 31 December 2016. Items are allocated to time bands by reference to the earlier of the next contractual interest rate change and the maturity date.

31 December 2016	Within 3 months £m	3 months but less than 6 months £m	6 months but less than 1 year £m	1 year but less than 5 years £m	More than 5 years £m	Non-interest bearing £m	Total £m
Assets							
Cash and balances at central banks	425.9	-	-	-	-	4.0	429.9
Loans and advances to banks	24.1	-	-	-	-	-	24.1
Loans and advances to customers	2,812.3	117.8	201.1	714.1	254.9	(49.8)	4,050.4
Derivative financial assets	-	-	-	-	-	5.2	5.2
Other non-financial assets	2.9	2.9	5.3	23.1	4.2	91.8	130.2
	3,265.2	120.7	206.4	737.2	259.1	51.2	4,639.8
Liabilities							
Customer deposits	1,191.2	954.8	630.7	1,166.8	-	-	3,943.5
Amounts due to banks	123.3	-	24.4	-	-	-	147.7
Derivative financial liabilities	-	-	-	-	-	0.4	0.4
Other non-financial liabilities	-	-	-	-	-	44.3	44.3
Subordinated debt liability	-	-	-	-	76.1	-	76.1
Total equity	-	-	-	-	-	427.8	427.8
	1,314.5	954.8	655.1	1,166.8	76.1	472.5	4,639.8
Notional values of derivatives	524.0	-	(340.0)	(145.0)	(39.0)	-	-
Interest rate sensitivity gap	2,474.7	(834.1)	(788.7)	(574.6)	144.0	(421.3)	-
Cumulative gap	2,474.7	1,640.6	851.9	277.3	421.3	-	-

30.4 Capital risk and management

Capital risk is the risk that the Group has insufficient capital to cover regulatory requirements and/or to support its own growth plans. Liquidity risk is the risk that the Group is not able to meet its financial obligations as they fall due, or can do so only at excessive cost.

The Group's objective in managing Group capital is to maintain appropriate levels of capital to support the Group's business strategy and meet regulatory requirements.

Policies and processes for managing the Group's capital

The Group's approach to capital management is driven by strategic and organisational requirements, while also taking into account the regulatory and commercial environments in which it operates.

The Group's principal objectives when managing capital are to:

address the expectation of the Shareholders and optimise business activities to ensure return on capital targets are achieved though efficient capital management;

ensure that the Group and Bank hold sufficient risk capital. Risk capital caters for unexpected losses that may arise, protects shareholders and depositors and thereby supports the sustainability of the Bank through the business cycles; and

comply with capital supervisory requirements and related regulations.

Risk management (continued)

The Prudential Regulation Authority (PRA) supervises the Group on a consolidated basis and receives information on the capital adequacy of, and sets capital requirements for, the Group as a whole. In addition, a number of subsidiaries are regulated for prudential purposes by either the PRA or the Financial Conduct Authority (FCA). The aim of the capital adequacy regime is to promote safety and soundness in the financial system and embed the requirements of Pillar 3 on market discipline. Under Pillar 2, the Group completes an annual self assessment of risks known as the Internal Capital Adequacy Assessment Process (ICAAP). The ICAAP is reviewed by the PRA which culminates in the PRA setting 'Individual Capital Guidance' (ICG) on the level of capital the Group and its regulated subsidiaries are required to hold. Pillar 3 requires firms to publish a set of disclosures which allow market participants to assess information on that firm's capital, risk exposures and risk assessment process. The Group's Pillar 3 disclosures can be found on the Group's website.

The Group maintains a strong capital base with the aim of supporting the development of the business and to ensure it meets the Pillar 1 capital requirements and ICG at all times. As a result, the Group maintains capital adequacy ratios above minimum regulatory requirements. The Group's individual regulated entities complied with all of the externally imposed capital requirements to which they are subject for the years ended 2017 and 2016.

Regulation

Capital Requirements Directive IV (CRD IV) requires the Group to hold Common Equity Tier 1 (CET1) capital to account for capital conservation, countercyclical and systemic risk buffers. A capital conservation buffer of 0.625% was introduced on 1 January 2016 and will increase each year to 2019 in line with regulations. The Bank's capital conservation buffer is currently set at 1.25%.

CRD IV also introduced a new leverage ratio requirement. The leverage calculation determines a ratio based on the relationship between Tier 1 capital and total consolidated exposure, being the sum of on-balance sheet exposures, derivative exposures, securities financing transaction exposures and off-balance sheet exposures. This leverage ratio is a risk-based measure that is designed to act as a supplement to risk-based capital requirements.

Minimum Requirements for Eligible Liabilities (MREL) are applicable from 1 January 2016 and will be phased in fully by 1 January 2020. Prior to 31 December 2019, MREL will be equal to an institution's minimum regulatory capital requirements. The Bank of England has provided MREL guidance to the Group, as well as guidance on the transitional arrangements until 1 January 2020.

The CET1 capital ratio for the Group was 12.8% as at 31 December 2017 (31 December 2016: 13.2%), compared with a regulatory minimum of 4.5%. The Total Tier 1 capital ratio for the Group was 16.5% as at 31 December 2017 (31 December 2016: 13.2%), compared with a regulatory minimum of 6.0%.

The leverage ratio for the Group (based on the Basel III definition of January 2014, and the revised EU capital requirements directive (CRD IV) definition of October 2014) is 9.4% (2016: 7.7%). The Group is not required to comply with the PRA leverage ratio framework until its retail deposits exceed the £50 billion threshold; however, the Group maintains a prudent risk appetite for leverage.

The Bank has a Pillar 2A requirement of 2.50% of risk-weighted assets.

Risk management (continued)

The following shows the regulatory capital resources managed by the Group and Bank:

	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Share capital	**175.5**	**175.5**	175.5	175.5
Share premium account	**81.0**	**81.0**	81.0	81.0
Capital redemption reserve	**16.7**	**16.7**	9.2	9.2
Merger reserve	**1.6**	**1.6**	1.6	1.6
Retained earnings	**215.2**	**201.2**	160.5	145.8
Intangible assets	**(59.4)**	**(44.6)**	(53.6)	(38.8)
Foreseeable dividend[1]	**-**	**-**	(6.7)	(6.7)
Common Equity Tier 1 capital	**430.6**	**431.4**	367.5	367.6
Capital securities	**125.0**	**125.0**	-	-
Additional Tier 1 capital	**125.0**	**125.0**	**-**	**-**
Total Tier 1 capital	**555.6**	**556.4**	**367.5**	**367.6**
Subordinated debt liability[2]	**75.0**	**75.0**	76.1	76.1
Collective impairment allowance	**11.1**	**11.0**	8.7	8.7
Tier 2 capital	**86.1**	**86.0**	84.8	84.8
Total regulatory capital	**641.7**	**642.4**	452.3	452.4

[1] As required by Article 26(2) of the Capital Requirements Regulation, a deduction was made for foreseeable dividends from the 2016 profit.
[2] Excludes capitalised interest of £1.1 million (2016: £nil). Accrued interest is payable semi-annually, and therefore excluded from capital reserves.

	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Risk-weighted assets[1]				
Property Finance	**1,529.1**	**1,529.1**	1,107.1	1,107.1
Business Finance	**967.2**	**945.3**	1,019.7	1,019.7
Consumer Lending	**489.8**	**489.8**	372.9	372.9
Other	**71.6**	**66.7**	66.9	66.9
Operational risk	**304.0**	**304.5**	212.0	212.0
	3,361.7	**3,335.4**	2,778.6	2,778.6

[1] Risk-weighted assets are not covered by the external auditor's opinion.

Risk management (continued)

The regulatory capital reconciles to the total capital in the Group's consolidated statement of financial position as follows:

	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Total regulatory capital	**641.7**	**642.4**	452.3	452.4
Subordinated debt liability[1]	**(75.0)**	**(75.0)**	(76.1)	(76.1)
Collective impairment allowance	**(11.1)**	**(11.0)**	(8.7)	(8.7)
Intangible assets	**59.4**	**44.6**	53.6	38.8
Foreseeable dividend[2]	**-**	**-**	6.7	6.7
Total equity	**615.0**	**601.0**	427.8	413.1

[1] Excludes capitalised interest of £1.1 million. Accrued interest is payable semi-annually, and therefore excluded from capital reserves.
[2] As required by Article 26(2) of the Capital Requirements Regulation, a deduction was made for foreseeable dividends from the 2016 profit.

The key capital ratios for the Group are presented below[1]:

	Group 2017	Company 2017	Group 2016	Company 2016
Common Equity Tier 1 capital ratio	**12.8%**	**12.9%**	13.2%	13.2%
Total Tier 1 capital ratio	**16.5%**	**16.7%**	13.2%	13.2%
Total capital ratio	**19.1%**	**19.3%**	16.3%	16.3%
Leverage ratio	**9.4%**	**9.5%**	7.7%	7.7%

[1] The Group's capital ratios are not covered by the external auditor's opinion.

The following table shows the movement in Total Tier 1 capital during the year:

	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Total Tier 1 capital at 1 January	**367.5**	**367.6**	308.9	308.6
Movement in Common Equity Tier 1 capital:				
Increase in capital redemption reserve	**-**	**7.5**	-	4.8
Movement in retained earnings:				
Profit for the year	**74.2**	**74.9**	65.7	66.1
Dividend paid	**(19.5)**	**(19.5)**	-	-
Share-based payments	**7.5**	**-**	4.8	-
Increase in intangible assets	**(5.8)**	**(5.8)**	(5.2)	(5.2)
Decrease/(increase) in foreseeable dividend[1]	**6.7**	**6.7**	(6.7)	(6.7)
Movement in Additional Tier 1 capital:				
Increase in capital securities	**125.0**	**125.0**	-	-
Total Tier 1 capital at 31 December	**555.6**	**556.4**	367.5	367.6

[1] As required by Article 26(2) of the Capital Requirements Regulation, a deduction was made for foreseeable dividends from the 2016 profit.

Risk management (continued)

Leverage ratio[1]	Group 2017 £m	Company 2017 £m	Group 2016 £m	Company 2016 £m
Total Tier 1 capital	**555.6**	**556.4**	367.5	367.6
Exposure measure:				
Total regulatory statement of financial position assets (excluding derivatives)	**5,750.2**	**5,699.6**	4,634.6	4,619.8
Exposure value for securities financing transactions	**-**	**-**	0.6	0.6
Off-balance sheet items	**224.7**	**224.7**	171.6	171.6
Exposure value for derivatives	**2.2**	**2.2**	1.3	1.3
Other regulatory adjustments	**(59.4)**	**(44.6)**	(59.9)	(38.8)
Total exposures	**5,917.7**	**5,881.9**	4,748.2	4,754.5
Leverage ratio	**9.4%**	**9.5%**	7.7%	7.7%

[1] The Group's leverage ratio is not covered by the external auditor's opinion

Exposure values associated with derivatives and securities financing transactions have been reported in compliance with CRD IV rules. For purposes of the leverage ratio, the derivative measure is calculated as the replacement cost for the current exposure plus an add-on for future exposure and is not reduced for any collateral received or grossed up for collateral provided.

Off-balance sheet exposure comprises of pipeline and committed facilities balances which have a credit conversion factor of medium risk attached to them.

Other regulatory adjustments comprise of net replacement costs of derivatives and securities financing transactions to the leverage ratio exposure.

31. Subsidiary companies

Accounting policy
Subsidiaries
Subsidiaries are entities controlled by the Group. The financial statements of the subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

The Company has the following subsidiary companies whose results are included in these consolidated financial statements:

	Country of incorporation	Class of shares held	Ownership %	Principal activity
Shawbrook International Limited	Jersey	Ordinary	100%	Banking
Shawbrook Buildings and Protection Limited	England and Wales	Ordinary	100%	FCA authorised introducer of insurance
Singers Corporate Asset Finance Limited	England and Wales	Ordinary	100%	Dormant
Singers Healthcare Finance Limited	England and Wales	Ordinary	100%	Dormant
Coachlease Limited	England and Wales	Ordinary	100%	Dormant
Hermes Group Limited	England and Wales	Ordinary	100%	Dormant
Singer & Friedlander Commercial Finance Limited	Scotland	Ordinary	100%	Dormant
Link Loans Limited	England and Wales	Ordinary	100%	Non-trading
Centric Group Holdings Limited	England and Wales	Ordinary	100%	Dormant
and its subsidiaries:				
Centric Group Finance 2 Limited	England and Wales	Ordinary	100%	Dormant
Centric Group Finance Limited	England and Wales	Ordinary	100%	Dormant
and its subsidiaries:				
Centric Commercial Finance Limited	England and Wales	Ordinary	100%	Dormant
Centric SPV 1 Limited	England and Wales	Ordinary	100%	Dormant
Centric SPV 2 Limited	England and Wales	Ordinary	100%	Dormant
Resource Partners SPV Limited	England and Wales	Ordinary	100%	Dormant

All entities have the same registered address as the Company, except the following:
Shawbrook International Limited – 1st Floor Kensington Chambers, Kensington Place, St Helier, JE4 0ZE, Jersey; and Singer & Friedlander Commercial Finance Limited – 8 Nelson Mandela Place, Glasgow, Scotland, G2 1BT.

32. Related party transactions

Related parties of the Group include Directors, key management personnel, close family members of Directors and key management personnel and entities which are controlled, jointly controlled or significantly influenced, or for which significant voting power is held, by Directors, key management personnel or their close family members.

Company
Movement in amounts owed by Group companies:

	2017	2016
	£m	£m
Balance at 1 January	**1.7**	2.6
Issue of capital securities	**125.0**	-
Investment in subsidiaries	**(125.0)**	-
Dividend paid to Shawbrook Group plc	**19.5**	-
Professional fees and other costs	**(17.8)**	0.3
Transfer of funds	**(2.4)**	(1.2)
Balance at 31 December	**1.0**	1.7

In 2015, Shawbrook Bank Limited entered into a £75 million subordinated debt with its parent, Shawbrook Group plc. The terms and conditions mirror the subordinated debt listed by Shawbrook Group plc on the London Stock Exchange on 28 October 2015 (see Note 25).

During 2017, Shawbrook Bank Limited issued £125.0 million Fixed Rate Reset Perpetual Additional Tier 1 Write Down Capital Securities to Shawbrook Group plc, on consistent terms as the securities (see Note 27) issued by Shawbrook Group plc and listed on the Irish Stock Exchange on 8 December 2017.

Pollen Street Capital Limited is a private equity firm who, in conjunction with BC Partners LLP, hold equal shareholdings in Marlin Bidco, the owner of Shawbrook Group plc.

During 2017, the Group entered into a €20 million revolving credit facility with Capitalflow (Asset Finance) DAC, which is 100% owned by PSC Nominee 3 Limited, a Pollen Street Capital Limited company. As of 31 December 2017, the balance outstanding was £5.8 million.

During 2017, the Group had a senior revolving facility with 1st Stop Funding Limited, whose ultimate parent is 1st Stop Holdings Limited. 1st Stop Holdings Limited is 100% owned by PSC Nominee 3 Limited, a Pollen Street Capital Limited company. The balance outstanding at 31 December 2017 was £20.0 million (2016: £21.0 million).

Transactions with Directors
The Directors of the Group declared and sold shares as part of the acquisition of Shawbrook Group plc by Marlin Bidco which totaled 4,447,746 shares of four Directors and two closely associated persons. Lindsey McMurray and Cédric Durbourdieu are Directors of Marlin Bidco Limited, Shawbrook Group's 100% shareholder.

Transactions with key management personnel
Key management personnel are defined as the Executive management team of the Group excluding the Executive and Non-Executive Directors. The total remuneration which included short-term benefits and employer pension contributions totalled £5.0 million (2016: £2.4 million). Six members of the Executive management team and two persons closely associated also declared and sold shares as part of the acquisition of the Group by Marlin Bidco which totalled 2,098,741 shares.

33. Capital commitments

The Group had capital commitments totalling £nil at 31 December 2017 (2016: £0.3 million).

34. Contingent liabilities and guarantees

Accounting policies
Financial guarantee contracts
Liabilities under financial guarantee contracts which are not classified as insurance contracts are recorded initially at their fair value, which is generally the fee received or the present value of the fee receivable. Subsequently, financial guarantee liabilities are measured at the higher of the initial fair value, less cumulative amortisation, and the best estimate of the expenditure required to settle the obligations.

Contingent liabilities
Contingent liabilities, which includes contingent liabilities related to legal proceedings or regulatory matters, are possible obligations that arise from past events whose existence will be confirmed only by the occurrence, or non-occurrence, of one or more uncertain future events not wholly within the control of the Group; alternatively they are present obligations that have arisen from past events but are not recognised because it is not probable that settlement will require the outflow of economic benefits, or because the amount of the obligations cannot be reliably measured. Contingent liabilities are not recognised in the financial statements but are disclosed unless the probability of settlement is remote.

Financial guarantee contracts
In 2015, the Group entered into a financial guarantee contract to an amount of £2.5 million. This contract is a continuous obligation which may be terminated by the Group on giving three months written notice. The contract is fully collateralised through a first fixed charge over a blocked deposit account to an amount of £2.5 million.

Contingent liabilities
Part of the Group's business is regulated by the Consumer Credit Act (CCA), which contains very detailed and highly technical requirements. The Group continues to commission external reviews of its compliance with the CCA and other consumer regulations. The Group has identified some areas of potential non-compliance, although these are not considered to be material. While the Group considers that no material present obligation in relation to non-compliance with the CCA and other consumer regulations is likely, there is a risk that the eventual outcome may differ.

The Group's Consumer Lending division is exposed to risk under Section 75 CCA, in relation to any misrepresentations or breaches of contract by suppliers of goods and services to customers where the purchase of those goods and services is financed by the Group. While the Group would have recourse to the supplier in the event of such liability, if the supplier becomes insolvent then that recourse would have limited value.

In 2017 the Group's Consumer Lending division has seen an increase in the number of customer complaints relating to the provision of solar panels by certain suppliers. These complaints relate either to the quality of the panels or to representations allegedly made by suppliers as to the expected financial performance of the panels and the Group investigates each complaint on its individual merits.

35. Ultimate parent company

The Company is a subsidiary undertaking of its ultimate parent company, Shawbrook Group plc, which is incorporated in England and Wales and is the largest company in which the results of the Company and its subsidiaries are consolidated. The consolidated financial statements of the Group are available on request from Lutea House, Warley Hill Business Park, Brentwood, Essex CM13 3BE.

36. Country-by-country reporting (CBCR)

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 came into effect on 1 January 2014 and place certain reporting obligations on financial institutions that are within the scope of the EU Capital Requirements Directive IV (CRD IV).

The objective of the CBCR requirements is to provide increased transparency regarding the source of the financial institution's income and locations of its operations.

Shawbrook Bank Limited and its subsidiaries are all UK or Channel Island registered entities, the activities of which are disclosed in Note 31.

The Group's net operating income, profit before taxation, income tax charge and number of full-time equivalent employees were:

	2017	2016
Net operating income (£m)	**238.1**	209.7
Profit before tax (£m)	**99.5**	89.1
Income tax charge (£m)	**25.3**	23.4
Tax paid (£m)	**29.5**	20.5
Average number of employees on a full-time equivalent basis	**671**	569

The Group did not receive any public subsidies.

37. Post-balance sheet events

On 23 February 2018, the Group received confirmation of an interim payment of £4.95 million relating to the Group's insurance claim in respect of the controls breach identified in the Business Finance Division in H1 2016, which will be paid subject to verification of the quantum of the claimed losses. The Group's insurers confirmed that the Group's insurance claim is covered in principle under the policy, but insurers are still considering certain aspects of the Group's claim before the final settlement amount can be determined.

There have been no other significant events between 31 December 2017 and the date of approval of the financial statements which would require a change to or additional disclosure in the financial statements.

Glossary

ALCo	Asset and Liability Committee.
Average Principal Employed	Calculated as the average of monthly closing loans and advances to customers, net of impairment provision, from the Group's financial reporting and management information systems, including operating leases, which are classified as property, plant and equipment in the Group's statutory accounts.
BAC	Board Audit Committee.
BRC	Board Risk Committee.
Basel II	The capital adequacy framework issued by the Basel Committee on Banking Supervision in June 2006 in the form of the 'International Convergence of Capital Measurement and Capital Standards'.
Basel III	Global regulatory standard on bank capital adequacy, stress testing and market and liquidity proposed by the Basel Committee on Banking Supervision in 2010. It aims to strengthen regulation, supervision and risk management in the banking sector. See also CRD IV.
Basis Point (bps)	One hundredth of a percent (0.01%). 100 basis points is 1%. It is used in quoting interest rates or yields on securities.
BBA	British Bankers Association, the leading trade association for the UK banking sector.
Board	The Board of Directors of Shawbrook Bank Limited
BoE	Bank of England.
Buy-to-let Mortgages	Buy-to-let mortgages are those mortgages offered to customers purchasing residential property as a rental investment.
Capital Requirements Regulation (CRR)	The European Union has implemented the Basel III capital proposals through the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), collectively known as CRD IV. CRD IV was implemented on 1 January 2014.
CCA	Consumer Credit Act.
Code	The FRC's UK Corporate Governance Code (2014 edition).
Common Equity Tier 1 Capital (CET1)	The highest quality form of capital under CRD IV that comprises common shares issued and related share premium, retained earnings and other reserves excluding the cash flow hedging reserve, less specified regulatory adjustments.
Common Equity Tier 1 Ratio (CET1 Ratio)	The Common Equity Tier 1 ratio is calculated as common equity tier 1 capital divided by risk-weighted assets.
Cost of Risk	Cost of risk is calculated as impairment losses on financial assets divided by average principal employed.
Cost to Income Ratio	Cost to Income Ratio is calculated as administrative expenses plus provisions for liabilities and charges, divided by net operating income.
CRD	Capital Requirements Directive.
CRD IV	In June 2013, the European Commission published legislation for a Capital Requirements Directive (CRD) and Capital Requirements Regulations (CRR) which form the CRD IV package. The package implements the Basel III proposals in addition to the inclusion of new proposals on sanctions for non-compliance with prudential rules, corporate governance and remuneration. The rules are implemented in the UK via the PRA policy statement PS7/13 and came

	into force from 1 January 2014, with certain sections subject to transitional phase in.
Customer Deposits	Monies deposited by individuals and companies that are not credit institutions. Such funds are recorded as liabilities in the Group's Statement of Financial Position.
Customer Loans	Loans and advances to customers, net of impairment provision and including operating leases, which are classified as property, plant and equipment in the Group's statutory accounts.
Deferred Tax Assets	Income taxes recoverable in future periods as a result of deductible temporary differences (temporary differences between the accounting and tax base of an asset or liability that will result in tax deductible amounts in future periods) and the carry forward of tax losses and unused tax credits.
Earnings at Risk (EaR)	Approach set out for the quantification of interest rate risk expressed as the impact of the sensitivity analysis on the change to net interest income.
EBA	European Banking Authority.
Effective Interest Rate Method (EIRM)	The effective interest rate method calculates the amortised cost of a financial asset or financial liability, and allocates the interest income over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash receipts through the expected life of the financial asset or financial liability. Calculation of the effective interest rate takes into account all contractual terms of the financial instrument but includes all amounts received or paid that are an integral part of the overall return, direct incremental transaction costs related to the acquisition or issue of a financial instrument and all other premiums and discounts.
Encumbrance	The use of assets to secure liabilities, such as by way of a lien or charge.
EPS	Earnings per share.
European Securities & Market Authority (ESMA)	An independent European Supervisory Authority with the remit of enhancing the protection of investors and reinforcing stable and well-functioning financial markets in the European Union.
Expected Loss (EL)	A measure of anticipated loss for exposures captured under an internal ratings based credit risk approach. The 12-month expected loss amount is the exposure, arising from a potential default of a counterparty, over the next 12 months in respect of the amount expected to be outstanding at default.
Exposure at Default	An estimate of the amount expected to be owed by a customer at the time of a customer's default.
Fair Value	The amount for which an asset could be exchanged, or a liability settled, between willing parties in an arm's length transaction.
FCA	Financial Conduct Authority.
Financial Services Compensation Scheme (FSCS)	The Financial Services Compensation Scheme is the UK's independent statutory compensation fund for customers of authorised financial service firms and pays compensation if a firm is unable to pay claims against it. The FSCS is funded by management expenses levies and, where necessary, compensation levies on the authorised firms.
Forbearance	Forbearance takes place when a concession is made on the contractual terms of a loan in response to borrowers' financial difficulties. Forbearance options are determined by assessing the customer's personal circumstances.
FRC	Financial Reporting Council.

Full-Time Equivalent (FTE)	A full-time employee is one that works a standard five-day week. The hours worked by part-time employees are measured against this standard and accumulated along with the number of full-time employees and counted as full-time equivalents.
Funding for Lending Scheme (FLS)	The Bank of England launched the Funding for Lending scheme in 2012 to allow banks and building societies to borrow from the Bank of England at cheaper than market rates for up to four years. This was designed to increase lending to businesses by lowering interest rates and increasing access to credit.
Group	The Company and its subsidiaries.
Gross Yield	Gross yield is calculated as the sum of interest and similar income, net income from operating leases, net fee and commission income and fair value gains/(losses) on financial instruments divided by average principal employed.
HIL	Home Improvement Loan.
HOL	Holiday Ownership Loan.
IFRS	International Financial Reporting Standards.
Impaired Assets	Loans that are in arrears or where there is objective evidence of impairment and where the carrying amount of the loan exceeds the expected recoverable amount. This definition also includes unsecured loans in the Consumer Lending division that are more than 90 days in arrears and carry identified impairment that is calculated on a collective basis.
Impairment Allowance	The impairment allowance includes allowances against loans that have been individually impaired and those that are subject to collective impairment.
Instalment credit agreement	An instalment credit agreement is an agreement similar in nature to a hire purchase agreement or otherwise known as a rent-to-own agreement.
Interest Rate Risk	The risk of a reduction in the present value of the current statement of financial position or earnings as a result of adverse movement in interest rates.
Internal Capital Adequacy Assessment Process (ICAAP)	The Group's own assessment, based on Basel III requirements, of the levels of capital that it needs to hold in respect of its regulatory capital requirements (for credit, market and operational risks) and for other risks including stress events as they apply on a solo level and on a consolidated level.
Internal Liquidity Adequacy Assessment Process (ILAAP)	The Group's own assessment of its overall liquidity adequacy and in particular the level of liquidity resources it requires to meet its liabilities as they fall due even under stressed conditions, in accordance with the Prudential Regulation Authority's liquidity rules under PS11/15.
International Organization of Securities Consensus (IOSCO)	The international body that brings together the world's securities regulators and is recognised as the global standard setter for the securities sector. IOSCO develops, implements and promotes adherence to internationally recognised standards for securities regulation.
IASB	International Accounting Standards Board.
IMF	International Monetary Fund.
IPO	Initial Public Offering.
Leverage Ratio	The leverage ratio is calculated Common Equity Tier 1 capital divided by the sum of total assets (excluding intangible assets and include adjustments for certain off-balance sheet items such as pipeline and undrawn collateral).
Liability yield	Liability yield is calculated as interest expense and similar charges divided by average principal employed.

LIBOR (London Inter-Bank Offered Rate)	The interest rate participating banks offer to other banks for loans on the London market.
Liquidity Coverage Ratio (LCR)	The ratio of the stock of high quality liquid assets to expected net cash outflows over the following 30 days. High quality liquid assets should be unencumbered, liquid in markets during a time of stress, and ideally, central bank eligible.
Liquidity Ratio	Liquidity ratio is calculated as the liquidity reserve divided by customer deposits. The liquidity reserve comprises cash and balances at central banks (excluding mandatory balances held with central banks), loans and advances to banks, off-balance sheet T-Bills but excludes additional available liquidity from pre-positioned assets.
Loan-to-Deposit Ratio	Calculated as loans and advances to customers divided by customer deposits.
Loss Emergence Period	The loss emergence period is the estimated period between impairment occurring and the loss specifically identified and evidenced by the establishment of an appropriate impairment allowance.
Loss Given Default	The estimated loss that will arise if a customer defaults. It is calculated after taking account of credit risk mitigation and includes the cost of recovery.
Management expenses ratio	Management expenses ratio is calculated as administrative expenses plus provisions for liabilities and charges, divided by average principal employed.
MCD	Mortgage Credit Directive.
MLRO	A Money Laundering Reporting Officer (MLRO) is the officer nominated within a firm or practice to make disclosures to the Serious Organised Crime Agency (SOCA) under the Proceeds of Crime Act 2002 and the Terrorism Act 2000.
Neither past due nor impaired	Loans that are not in arrears and which do not meet the impaired asset definition. This segment can include assets subject to forbearance solutions.
Net Interest Income	The difference between interest received on assets and interest paid on liabilities.
Net Interest Margin (NIM)	Calculated as net operating income divided by average principal employed.
Net Stable Funding Ratio (NSFR)	The ratio of Available Stable Funding required to support the assets and activities over the medium term as set out by the Basel III requirements and implemented by the EBA and the PRA
NPL Ratio	The NPL ratio is calculated by adding past due over 90 days loans and advances to customers and impaired loans and advances to customers and dividing the sum by total gross loans and advances to customers.
NPL Provision Coverage Ratio	Calculated as statement of financial position impairment provision as a percentage of past due over 90 days loans and advances to customers and impaired loans and advances to customers.
OBR	Office for Budget Responsibility.
Past due	A loan is considered past due when the borrower has failed to make a payment under the terms of the loan agreement. This may also include loans past maturity where an outstanding balance exists.
Past due but not impaired	Loans past due but not impaired consist predominantly of loans in Property Finance and Business Finance that are impaired. This definition also included unsecured loans in the Consumer Lending Division that are past due but not more than 90 days.
Pillar 1	The part of the Basel framework that sets outs the rules that govern the calculation of Minimum capital requirements for credit, market and operational

	risks.
PRA	Prudential Regulation Authority.
PSP	Performance Share Plan.
Recovery Plan and Resolution Pack (RP&RP)	The Bank Recovery and Resolution Directive (BRRD) establishes a common approach to the recovery and resolution of banks and investment firms. The Group's Recovery Plan enables the Board and senior management to manage a crisis which may threaten the capital and/or liquidity adequacy of the Bank, or its ultimate viability. The objective of the plan is to put in place measures (recovery options) to restore capital, liquidity or profitability so that the Bank can operate sustainably and viably. The Group's Resolution Pack lays out the information required to support effective resolution planning. The requirements for the Recovery Plan and Resolution Pack are set out in supervisory statement SS18/13 and SS19/13 respectively.
Repurchase Agreements or 'Repos'	An agreement where one party, the seller, sells a financial asset to another party, the buyer, at the same time the seller agrees to reacquire and the buyer to resell the asset at a later date. From the seller's perspective, such agreements are repurchase agreements (repos) and from the buyer's perspective they are reverse repurchase agreements (reverse repos).
Return on Lending Assets	Return on lending assets before tax is calculated as profit/(loss) before taxation divided by average principal employed.
Return on Tangible Equity (RoTE)	Return on tangible equity is calculated as profit for the year attributable to owners divided by average tangible equity. Average tangible equity is calculated as total equity less intangible assets at the beginning of a period plus total equity less intangible assets at the end of the period, divided by two.
Risk-weighted Assets	A measure of a bank's assets adjusted for their associated risks. Risk weightings are established in accordance with PRA rules and are used to assess capital requirements and adequacy under Pillar 1.
Secured Lending	Lending on which the borrower uses collateral such as equity in their home.
Standardised Approach	In relation to credit risk, a method for calculating credit risk capital requirements using External Credit Assessment Institutions (ECAI) ratings of obligators (where available) and supervisory risk weights. In relation to operational risk, a method of calculating the operational risk capital requirement by the application of a supervisory defined percentage charge to the gross income of specified business lines.
Stress Testing	Stress and scenario testing is the term used to describe techniques where plausible events are considered as vulnerabilities to ascertain how this will impact the capital or liquidity resources which are required to be held.
Term Funding Scheme (TFS)	The Bank of England launched the Term Funding Scheme in 2016 to allow banks and building societies to borrow from the Bank of England at rates close to Bank Base Rate. This is designed to increase lending to businesses by lowering interest rates and increasing access to credit.
Tier 1 Capital	A measure of banks financial strength defined by the PRA. It captures Common Equity Tier 1 capital plus other Tier 1 securities in issue, but is subject to a deduction in respect of material holdings in financial companies.
Tier 1 Capital Ratio	Tier 1 capital as a percentage of risk-weighted assets.
Tier 2 Capital	A further component of regulatory capital defined by the PRA. It comprises eligible collective assessed impairment allowances under CRD IV.
Total Capital Ratio (TCR)	The Total Capital Ratio is calculated as total regulatory capital divided by risk-weighted assets.

TNAV	Tangible Net Asset Value.
Unencumbered Assets	Assets that are readily available to secure funding or to meet collateral requirements, and assets that are not subject to any restrictions but are not readily available for use.