Nemo Personal Finance Limited

Annual report for the year ended
31 December 2019

Registered Number: 05188059

Annual report
for the year ended 31 December 2019

Contents

Officers and professional advisers

Directors	I A Mansfield T Denman J S Mycroft (resigned 30 November 2019)
Secretary	C Cooper
Registered office	Principality Buildings Queen Street Cardiff Wales CF10 1UA
Bankers	Barclays Bank Plc 3rd Floor Windsor Court Windsor Place Cardiff Wales CF10 3BX
Solicitors	Eversheds Sutherland LLP 1 Callaghan Square Cardiff Wales CF10 5BT
Auditors	Deloitte LLP 5 Callaghan Square Cardiff Wales CF10 5BT

Strategic report
for the year ended 31 December 2019

Strategic Report

Nemo Personal Finance Limited continued to perform as expected, fulfilling an important role within the Principality Building Society group.

The Company ceased accepting new business in March 2016. Following a successful transition from lender to servicer, the business has delivered a solid set of results in 2019, continuing to focus on delivering good customer outcomes and robust cost management.

Key performance indicators

Year ended 31 December	2019	2018
Profit before tax (£000's)	13,046	11,915
Profit before tax as a % of mean assets	6.27%	4.3%
Total assets (£000's)	179,622	236,399
Change in total assets	(23.9)%	(24.3)%
Non-performing loans (6+ months in arrears) (£000's)	4,603	5,515
Non-performing loans (6+ months in arrears) (volume)	151	181
Yield %	9.0%	9.0%

Business review

The Company saw a increase in profit in 2019, with profit before tax of £13.0m (2018: £11.9m). This is largely due to recoveries against previously impaired loan assets, including a £1.3m gain from the sale of an unsecured portfolio of loans to a third party during the year.

Loans in the portfolio continue to demonstrate strong credit quality with a low level of impairment. Arrears performance across the portfolio and continued run-off of the book has reduced the impairment provision held in the statement of financial position to £6.5m (2018: £8.9m).

Interest margin, the effective interest earned on loans to customers after deducting funding costs, was broadly in line with the prior year at 5.1% (2018: 5.2%).

The Company offers a range of account management and forbearance options for the borrower. In the event of short-term difficulty, the Company operates temporary reductions in payments and 'rehabilitation' tools for borrowers in arrears or pre-delinquency.

Principal risks and uncertainties

The Company's operations expose it to a variety of financial and non-financial risks that include the effects of credit risk, conduct risk, liquidity risk and operational risk.

The key risks to the Company are linked to the overall performance of the economy and the resultant effect on interest rates, unemployment and house price indices, together with customer and conduct risks. Overall risk is managed in line with the Parent's policy and further information on this can be found in the Principality Building Society financial statements in the Risk Overview section of the Strategic Report.

Strategic report
for the year ended 31 December 2019 (continued)

Credit risk

Credit risk is the risk that a customer or counterparty will fail to meet their financial obligations to the Company as they become due. Credit risk policies were in place to reduce the risk of lending to retail customers who may be unable to afford to repay the loans. The credit risk policy had a number of criteria in relation to income, debt to income ratio, loan to value ratio and credit score to minimise the credit risk.

Conduct risk

Conduct risk is the risk that the Company does not treat its customers fairly, resulting in inappropriate or unfair outcomes. The sustainability of the Company's business model and the achievement of its strategy are dependent upon the consistent and fair treatment of customers. Furthermore, the regulatory regime in the UK continues to highlight the importance of firms' conduct and their approach to deliver fair customer outcomes. Consequently, the Company continues to focus heavily on its risk and control framework to manage conduct risks. Oversight is provided by the Group's Board Risk Committee and the Group's Compliance and Conduct function.

Liquidity risk and capital management

Liquidity risk is the risk that the Company has insufficient funds to meet its obligations as and when they fall due. The Parent monitors risk exposure and the reporting of liquidity risk takes the form of cash flow measurement. Sources of liquidity are regularly reviewed by the Finance Committee.

Operational risk

Operational risk is the risk of loss arising from inadequate or failed internal processes, systems, human error or from external events.

The Parent has an established operational risk management framework which is utilised to identify, assess and monitor operational risk, including fraud, system failure, cyber threats and business continuity. The assessment of exposure to operational risks is based on both quantitative and qualitative considerations. Appropriate strategies are in place to manage and mitigate the risks that could impact the Company's ability to meet its business objectives whilst protecting its reputation. The crystallisation of operational risks is captured through the recording of operational losses and near misses. The analysis of loss events is used to identify any potential systemic weaknesses in operational processes. Oversight is provided by the Operational Risk Committee.

Future developments

Total assets and profits are expected to continue to reduce over time as the loan book runs off. The focus of the business will remain on providing a high level of service to customers whilst housekeeping the portfolio and managing the risks to which the Company is exposed.

Approved by the Board

I A Mansfield
Director
5 February 2020

Directors' report for the year ended 31 December 2019

The Directors present their report and the financial statements of the Company for the year ended 31 December 2019.

Principal activities

The principal activity of the Company is loan servicing.

Dividends and transfer to reserves

The results for the period are set out in the income statement. The Directors do not recommend the payment of a dividend (2018: £nil).

Going concern

The Parent, Principality Building Society, prepares forecasts, projections and scenario testing which includes Nemo Personal Finance Limited. These are carried out in accordance with the Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP). These processes are required by the regulators to demonstrate appropriate levels of capital and liquidity under stressed conditions. These take account of possible changes in trading performance and show that the Parent will be able to operate within the sources of funding currently available to it.

The Parent monitors its liquidity levels to ensure that an appropriate level of resources is maintained to meet the requirements of the business. These are assessed under a number of stressed scenarios reflecting the Directors' views of different risks that might arise under current economic conditions.

As presented in the statement of financial position, the Company has financial resources, including an intercompany loan from its Parent, which the Parent has confirmed it will not seek repayment in the next 18 months, to meet its day-to-day working capital requirements. The Company's forecasts, taking into account reasonable possible changes in trading performance, show that the Company will be able to operate within the sources of funding currently available to it.

Having considered the plans and forecasts for the Company and events up to and including the date of signing, the Directors believe that there are no material uncertainties that cast significant doubt on the Company's ability to continue in business for the foreseeable future. Accordingly, the financial statements continue to be prepared on a going concern basis.

Future developments and financial risk management objectives and policies have been disclosed within the Strategic Report on pages 4-5.

Directors

The current Directors of the Company are as shown on page 3. J S Mycroft resigned as a director on 30 November 2019.

The Company has made qualifying third party indemnity provisions for the benefit of its directors which remain in force at the date of this report.

Directors' report
for the year ended 31 December 2019 (continued)

Directors' responsibilities statement

The Directors are responsible for preparing the Annual Report and the financial statements in accordance with applicable law and regulations.

Company law requires the Directors to prepare financial statements for each financial year. Under that law the Directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. 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 Company and of the profit or loss of the Company for that period. In preparing these financial statements, International Accounting Standard 1 requires that Directors:

- properly select and apply accounting policies;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- provide additional disclosures when compliance with the specific requirements in IFRSs are insufficient to enable users to understand the impact of particular transactions, other events and conditions on the entity's financial position and financial performance; and
- make an assessment of the company's ability to continue as a going concern.

The Directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They are also responsible for safeguarding the assets of the Company and hence for taking reasonable steps for the prevention and detection of fraud and other irregularities.

Auditor

All Directors at the time of approving this report confirm the following:

(a) so far as each Director is aware, there is no information of which the Company's auditor is unaware, and

(b) each Director has taken all the steps they ought to have taken as a Director in order to make themselves aware of any relevant audit information, and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of S418 of the Companies Act 2006.

Deloitte LLP have expressed their willingness to continue in office as auditor and the Board of Directors has resolved that Deloitte LLP should be reappointed.

Approved by the Board

I A Mansfield
Director
5 February 2020

Independent Auditor's report to the members of Nemo Personal Finance Ltd

Report on the audit of the financial statements

Opinion

In our opinion the financial statements of Nemo Personal Finance Limited (the 'company'):

- give a true and fair view of the state of the company's affairs as at 31 December 2019 and of its profit for the year then ended;
- have been properly prepared in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

We have audited the financial statements which comprise:

- the income statement;
- the statement of changes in shareholders' equity;
- the statement of financial position;
- the statement of cash flows; and
- the related notes 1 to 22.

The financial reporting framework that has been applied in their preparation is applicable law and IFRSs as adopted by the European Union.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the auditor's responsibilities for the audit of the financial statements section of our report.

We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the Financial Reporting Council's (the 'FRC's') Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

We are required by ISAs (UK) to report in respect of the following matters where:

- the directors' use of the going concern basis of accounting in preparation of the financial statements is not appropriate; or
- the directors have not disclosed in the financial statements any identified material uncertainties that may cast significant doubt about the company's ability to continue to adopt the going concern basis of accounting for a period of at least twelve months from the date when the financial statements are authorised for issue.

We have nothing to report in respect of these matters.

Independent Auditor's report to the members of Nemo Personal Finance Ltd (continued)

Other information

The directors are responsible for the other information. The other information comprises the information included in the annual report, other than the financial statements and our auditor's report thereon. Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in our report, we do not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether there is a material misstatement in the financial statements or a material misstatement of the other information. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact.

We have nothing to report in respect of these matters.

Responsibilities of directors

As explained more fully in the directors' responsibilities statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the 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 the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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 error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

A further description of our responsibilities for the audit of the financial statements is located on the FRC's website at: http://www.frc.org.uk/auditorsresponsibilities. This description forms part of our auditor's report.

Report on other legal and regulatory requirements

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the strategic report and the directors' report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the strategic report and the directors' report have been prepared in accordance with applicable legal requirements.

Independent Auditor's report to the members of Nemo Personal Finance Ltd (continued)

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the strategic report or the directors' report.

Matters on which we are required to report by exception

Under the Companies Act 2006 we are required to report in respect of the following matters if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; 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 respect of these matters.

Use of our report

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.

K. J. Cooper

Kieren Cooper (Senior Statutory Auditor)
For and on behalf of Deloitte LLP
Statutory Auditor
Cardiff, United Kingdom
5 February 2020

Income statement
for the year ended 31 December 2019

Continuing operations:	**Notes**	**2019** **£'000**	**2018** **£'000**
Interest receivable and similar income	4	16,187	21,495
Interest payable and similar charges	5	(5,659)	(7,082)
Net interest income		**10,528**	**14,413**
Fees and commissions receivable		97	177
Fees and commissions payable		-	(45)
Net income		**10,625**	**14,545**
Impairment gain/(loss) on loans	10	3,716	(221)
Regulatory provisions	12	-	**33**
Operating expenses		(1,295)	(2,442)
Profit before taxation	6	**13,046**	**11,915**
Income tax expense	8	(2,225)	(2,282)
Profit for the financial year		**10,821**	**9,633**

There are no items of other comprehensive income and therefore no Statement of Other Comprehensive Income has been prepared.

The accounting policies and notes on pages 15 to 34 form part of these accounts.

Statement of changes in shareholders' equity for the year ended 31 December 2019

	Notes	2019 £'000	2018 £'000
Profit for the financial year		10,821	9,633
Net increase to shareholders' equity		**10,821**	**9,633**
Opening shareholders' equity at 1 January		94,839	84,387
Changes on initial application of IFRS 9		-	987
Tax effect of IFRS 9 implementation		-	(168)
Restated balance at 1 January		94,839	85,206
Closing shareholders' equity		**105,660**	**94,839**

The accounting policies and notes on pages 15 to 34 form part of these accounts.

Statement of financial position as at 31 December 2019

	Notes	2019 £'000	2018 £'000
Assets			
Loans and receivables	10	179,480	236,348
Deferred sale consideration	20	15	49
Deferred tax	14	46	2
Property, plant and equipment	9	81	-
Total assets		**179,622**	**236,399**
Liabilities			
Trade and other payables	11	1,377	1,735
Regulatory provisions	12	2,695	3,285
Short-term loans and overdrafts	13	348	287
Current tax		1,049	1,072
Long-term loans	13	68,493	135,181
Total liabilities		**73,962**	**141,560**
Equity			
Called up share capital	15	100	100
Retained profit		105,560	94,739
Total equity		**105,660**	**94,839**
Total equity and liabilities		**179,622**	**236,399**

The financial statements of Nemo Personal Finance Limited, registered number 05188059, on pages 11 to 34, were approved by the Board of Directors and authorised for issue on 5 February 2020.

I A Mansfield
Director

Statement of cash flows
for the year ended 31 December 2019

	Notes	2019 £'000	2018 £'000
Net cash inflow from operating activities:			
Cash from operating activities (see below)		66,971	83,780
Net cash from operating activities		**66,971**	**83,780**
Cash flows used in investment activities:			
Lease payments following IFRS 16 adoption		(344)	-
Net cash used in investing activities		**(344)**	**-**
Cash flows used in financing activities:			
Repayment of loan advanced by parent company	19	(66,688)	(83,580)
Net cash used in financing activities		**(66,688)**	**(83,580)**
Net (decrease)/increase in cash and cash equivalents		(61)	200
Cash and cash equivalents at start of year		(287)	(487)
Cash and cash equivalents at end of year		**(348)**	**(287)**
Cash and cash equivalents comprise:			
Short-term loans and overdrafts		**(348)**	**(287)**
Net cash inflow from operating activities:			
Profit for the year before tax	8	13,046	11,915
Adjusted for:			
Depreciation	6	123	-
Decrease in provision for impairment		(2,398)	(839)
Decrease in regulatory provision		(590)	(535)
Net decrease in loans and receivables		59,266	76,498
Decrease in deferred consideration and other assets		34	95
Decrease in trade and other payables		(217)	(1,421)
Equity adjustment for accounting policy changes		-	987
Tax paid		(2,293)	(2,920)
Net cash inflow from operating activities		**66,971**	**83,780**

Notes to the financial statements for the year ended 31 December 2019

1. Accounting policies

Basis of preparation

Nemo Personal Finance Limited is a private company limited by shares. The Company's financial statements for the year ended 31 December 2019 have been prepared in accordance with International Financial Reporting Standards (IFRS) and interpretations issued by the International Financial Reporting Interpretations Committee (IFRIC) as adopted by the European Union (EU). The financial statements are prepared under the historical cost convention except for certain financial assets held at fair value.

The financial statements have been prepared on a going concern basis. This is discussed in the Directors' Report on page 6, under the heading 'Going concern'.

New and amended standards adopted by the Company

The company has adopted IFRS 16 Leases with effect from 1 January 2019, the impact from which is set out below. IFRIC 23 Uncertainty over Income Tax Treatments was also adopted from 1 January 2019, with no significant impact on the financial statements. Adoption of amendments to existing standards and annual improvements did not have any impact on the company's accounting policies and did not require retrospective adjustments.

Adoption of IFRS 16 Leases

IFRS 16 specifies how an entity recognises, measures and presents leases. The standard provides a single lessee accounting model, requiring lessees to recognise assets and liabilities for all leases, including bringing those leases previously classified as 'operating leases' onto the balance sheet.

The Company has applied the modified retrospective transition approach, under which the value of the right of use asset is set equal to the value to the lease liability on the date of transition and there is no requirement to restate prior financial periods. In applying IFRS 16 for the first time, no significant practical expedients were taken.

The lease liability was measured as the present value of all remaining lease payments, discounted at the Company's incremental borrowing rate. However, the impact of discounting on transition was negligible due to the lease ending in August 2020. The impact of adopting IFRS 16 was to increase both assets and liabilities by £204k as at 1 January 2019.

Below is a reconciliation between operating lease commitments previously disclosed as at 31 December 2018 and the recognised lease liability at 1 January 2019.

	£'000
Operating lease commitments at 31 December 2018	873
Adjustments for:	
VAT on operating lease not recognised in right of use asset	(167)
Lease liability recognised as at 1 January 2019	**706**
Onerous lease already recognised	(502)
Right of use asset recognised on transition as at 1 January 2019	**204**

Notes to the financial statements for the year ended 31 December 2019 (continued)

1. Accounting policies (continued)

	1 January 2019 £'000
Right of use asset by type:	
Properties	706
Less: impairment previously recognised as an onerous lease	(502)
Right of use asset as at 1 January 2019	**204**

Prior to 1 January 2019, operating lease rentals payable were recognised as an expense in the income statement on a straight-line basis over the lease term, less any amounts previously recognised as an onerous lease. From 1 January 2019, all leases entered into are recognised as a right of use asset and a corresponding lease liability at the date on which the leased asset is available for use. Assets and liabilities arising from a lease are initially measured at the present value of the lease payments over the term of the lease, less provision for impairment. The lease payments are discounted using the interest rate implicit in the lease or, if that rate cannot be determined, the Company's incremental borrowing rate is used.

The finance cost is charged to the income statement so as to produce a constant periodic rate of interest on the remaining balance of the lease liability for each period. The right of use asset is depreciated over the shorter of the asset's useful life and the lease term on a straight-line basis.

Impact of standards issued but not yet applied

At the date of authorisation of these financial statements, a number of new standards and interpretations, which have not been applied in these financial statements, were in issue but not yet effective. None of these changes are expected to have a significant impact on the Company's financial statements.

Accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these financial statements, except where stated below.

(a) Revenue

Revenue primarily comprises interest receivable on customer loans outstanding. All revenue is derived in the UK.

Interest

Interest income or expense is recognised on all interest-bearing financial assets classified as loans and receivables, and on financial liabilities, using the effective interest method.

The effective interest rate is the rate that exactly discounts the expected future cash payments or receipts through the expected life of the financial instrument or, where appropriate, a shorter period, to the net carrying amount of the instrument. The application of the method has the effect of recognising income (and expense) receivable (or payable) on the instrument evenly in proportion to the amount outstanding over the period to maturity or repayment.

Notes to the financial statements for the year ended 31 December 2019 (continued)

1. Accounting policies (continued)

Fees and commissions payable are included in the calculation of the effective interest rate to the extent that they can be measured and are considered to be an integral part of the effective interest rate. The effective interest rate calculation therefore recognises commissions payable on day one to third parties for the introduction of loans and advances to customers; interest earned on loans settled earlier than the contractual maturity date; and other cash flows arising from the direct and incremental costs of issuing financial instruments over the expected life of the financial instrument.

(b) Classification and measurement of financial instruments

Financial assets

Financial assets comprise customer loans and receivables and deferred sale consideration.

At initial recognition, the Company measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss (FVTPL), transaction costs that are directly attributable to the acquisition of the financial asset. Transaction costs of financial assets carried at FVTPL are expensed in profit or loss. Thereafter, financial assets are classified and measured in one of the three following measurement categories:

- those to be measured at amortised cost;
- those to be measured subsequently at fair value through other comprehensive income (FVOCI); or
- those to be measured subsequently at fair value through profit or loss.

The classification and subsequent measurement of financial assets depends on the business model for managing the financial assets and the contractual terms of the cash flows.

- Amortised cost: Assets that are held for collection of contractual cash flows where those cash flows represent solely payments of principal and interest are measured at amortised cost using the effective interest method, net of provision for impairment. Interest earned from these financial assets is included in interest receivable and similar income. Impairment losses are presented as separate line item in the income statement.
- FVOCI: Assets that are held for collection of contractual cash flows and for selling the financial assets, where the assets' cash flows represent solely payments of principal and interest, are measured at FVOCI. Movements in fair value are taken through OCI and, on derecognition, the cumulative gain or loss previously recognised in OCI is reclassified to the income statement. Interest is recognised using the effective interest method and included in interest receivable and similar income.
- FVTPL: Assets that do not meet the criteria for amortised cost or FVOCI are measured at FVTPL.

Financial liabilities

Financial liabilities comprise short-term loans and overdrafts and long-term loans and are measured at fair value on initial recognition and thereafter at amortised cost using the effective interest method.

Notes to the financial statements for the year ended 31 December 2019 (continued)

1. Accounting policies (continued)

(c) Impairment losses on loans and receivables

In accordance with IFRS 9, the Company uses a three stage model for impairment based on changes in credit quality since initial recognition. Each stage represents a change in the credit risk of a financial instrument since origination. Credit risk is measured using probability of default (PD), exposure at default (EAD) and loss given default (LGD). If a significant increase in credit risk (SICR) since initial recognition is identified but the asset is not yet deemed to be credit impaired, the financial instrument is moved from stage 1 to stage 2. Financial instruments that are deemed to be credit impaired are moved to stage 3. This assessment is performed on a monthly basis.

Financial instruments in stage 1 have their expected credit loss (ECL) measured at an amount equal to the portion of lifetime expected credit losses that result from default events possible within the next 12 months. Financial instruments in stages 2 or 3 have their ECL measured based on expected credit losses on a lifetime basis.

Significant increase in credit risk

There are three main components to the staging criteria for the loan portfolio. In order to move from stage 1 to stage 2 a loan is required to meet at least one of the following criteria:

- Forbearance activity;
- PD grade deterioration over a predetermined threshold relative to the starting point; and
- 30 days past due.

Loans are moved from stage 2 to stage 3 when they are credit impaired. Loans are considered to be credit impaired if they are 90 days past due or the borrower has been declared bankrupt.

Subject to the characteristics of the borrower, a loan will move back from stage 2 or 3 following a reversal of the criteria described above.

Expected Credit Loss (ECL) models

Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- PD is the likelihood of a borrower defaulting on its financial obligation either in the next 12 months or over the remaining lifetime of the obligation.
- EAD is based on the amounts the Company expects to be owed at the time of default.
- LGD represents the Company's expectation of the extent of loss on defaulted exposures.

The PD is calculated via a behavioural scorecard approach, using internal account level specific data including arrears history and external credit profile data provided by credit reference agencies.

Forward-looking information in the ECL models

The assessment of SICR and the calculation of ECL both incorporate forward looking information. The Company has performed historical analysis and identified the economic variables impacting credit risk and expected credit losses for each portfolio. Forecasts of these economic variables together with probability weightings are supplied by an external provider. Economic scenarios are selected which take account of a range of possible economic outcomes.

Notes to the financial statements for the year ended 31 December 2019 (continued)

1. Accounting policies (continued)

(d) Cash and cash equivalents

For the purposes of the cash flow statement and statement of financial position, cash and cash equivalents comprise balances with less than three months' maturity from the date of acquisition, including: cash and non-restricted balances with central banks, treasury bills and other eligible bills, loans and advances to banks, other amounts due from banks and short-term government securities. For the purposes of the cash flow statement, the cash and cash equivalents balance is stated net of short-term loans and overdrafts.

(e) Provisions

Provisions are recognised when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle that obligation and a reliable estimate can be made of the amount of the obligation.

The amount recognised as a provision is the best estimate of the consideration required to settle the present obligation at the statement of financial position date, taking into account the risks and uncertainties surrounding the obligation. Where a provision is measured using the cash flows estimated to settle the present obligation, its carrying amount is the present value of those cash flows (when the effect of the time value of money is material).

(f) Taxes, including deferred taxes

Tax payable on taxable profits ("current tax") is recognised as an expense in the period in which the profits arise. Tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits. payable on taxable profits ("current tax") is recognised as an expense in the period in which the profits arise. Tax recoverable on tax allowable losses is recognised as an asset only to the extent that it is regarded as recoverable by offset against current or future taxable profits.

Deferred tax is provided in full, using the liability method, on temporary timing differences arising from the differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and legislation enacted or substantively enacted by the statement of financial position date and is expected to apply when the deferred tax asset is realised or the deferred tax liability is settled. tax is provided in full, using the liability method, on temporary timing differences arising from the differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred tax is determined using tax rates and legislation enacted or substantively enacted by the statement of financial position date and is expected to apply when the deferred tax asset is realised or the deferred tax liability is settled.

Deferred and current tax assets and liabilities are only offset when they arise in the same tax reporting group and where there is both the legal right and the intention to settle on a net basis or to realise the asset and settle the liability simultaneously

Notes to the financial statements for the year ended 31 December 2019 (continued)

2. Judgements in applying accounting policies and critical accounting estimates

There are no significant judgements made in applying the group's accounting policies. However, there are significant estimation uncertainties which affect the amounts recognised in the financial statements. Critical accounting estimates and assumptions are made that could affect the reported amounts of assets and liabilities within the following financial year.

The most significant areas where accounting estimates are made are as follows:

Impairment provision on loans and receivables

The critical accounting estimates applied in determining expected credit loss provisions are:

- determining criteria for identifying significant increase in credit risk.
- choosing appropriate models and assumptions for the measurement of expected credit losses; and
- establishing the number and relative weightings of forward-looking economic scenarios.

Critical estimates are reviewed on an ongoing basis as part of the Company's IFRS 9 model governance process.

Sensitivity analysis has been performed on the staging criteria and PD models. A 10% variance has been selected as this is deemed to be the maximum variation likely to occur over a 12 month period in the current economic environment. The impact of 10% of the loans currently in stage 1 moving to stage 2 and the impact of 10% of loans currently in stage 2 moving to stage 1 are as follows:

Stage	£'000
Stage 1 to stage 2	100
Stage 2 to stage 1	(200)

The impact of a 10% change to the PD rates would cause a £490k change in impairment provisions.

The IFRS 9 models calculate expected credit losses for each of the scenarios and then apply the relative weightings of the forward-looking economic scenarios to generate the weighted output for each model.

The scenarios consist of the following:

Scenario	Weighting at 31 December 2019 %	GDP Growth %	Unemployment growth %	House price growth %
Base	45	3.5	1.0	1.0
Stronger near term growth	-	4.6	(1.0)	4.0
Slower near term growth	25	2.7	1.0	(1.0)
Protracted slump	15	(0.5)	4.0	(7.0)
Stagflation	15	1.8	3.0	(3.0)

Notes to the financial statements for the year ended 31 December 2019 (continued)

2. Judgements in applying accounting policies and critical accounting estimates (continued)

The equivalent scenarios at 31 December 2018 were as follows:

Scenario	Weighting at 31 December 2018 %	GDP Growth %	Unemployment growth %	House price growth %
Base	44.7	1.5	0.8	1.3
Stronger near term growth	10.7	2.7	(0.6)	5.2
Mild recession	26.8	0.9	1.5	(0.6)
Protracted slump	7.1	(0.9)	4.3	(6.8)
Stagflation	10.7	(0.1)	3.1	(2.9)

In addition to applying the scenarios and weightings set out above, further allowance was made in the prior year for the impact of the UK not achieving an orderly exit from the EU by the deadline of 29 March 2019. This allowance totalled £1.7m at 31 December 2019.

Following developments in 2019, the remaining uncertainty in relation to Brexit has been captured within the weightings applied to the scenarios as set out above, with no additional allowance made. Within these, the decision has been taken to apply a zero weighting to stronger near term growth in the current year, in reflection of the political, economic and environmental uncertainty that exists both in the UK and globally at the time of drafting these financial statements.

Sensitivity analysis has been performed on the impact of the economic scenarios. The range of ECL impact between the most optimistic scenario and the most severe scenario is £5.9m (2018: £5.4m). The ECL range is the difference between applying a 100% weighting to the most severe downturn scenario and the most optimistic scenario.

Regulatory provisions

Regulatory provisions have been made in respect of various customer claims. At 31 December 2019, the Company held a provision of £2.7m (2018: £3.3m). This reflects management's best estimate of the costs required to settle its remaining obligations and takes account of:

- expected customer behaviour;
- costs incurred with associated legal claims; and
- an updated assessment of the remaining exposure population.

Although a significant degree of uncertainty remains with regard to the ultimate cost of settling customer claims, the provision balance is expected to be sufficient to meet any remaining obligations. The provision will continue to be monitored and customer trends and behaviour analysed in order ensure the provision remains appropriate. Further information is included in note 21.

Notes to the financial statements for the year ended 31 December 2019 (continued)

3. Operating segments

The Company operates a single material operating segment, secured personal lending. The Company operates entirely within the UK and therefore a geographical segment analysis is not required.

4. Interest receivable and other similar income

Interest income consists of interest receivable on customer loans and early settlement interest, less origination costs and commissions payable to third parties for the introduction of loans and advances to customers.

5. Interest payable and similar charges

Interest expense consists of interest and other charges payable on funding from the Parent.

6. Profit before taxation

	2019 £'000	2018 £'000
Depreciation of right of use asset	123	-

The depreciation of the right of use asset is as a result of the adoption IFRS 16 from 1 January 2019.

There were no non-audit services received in either the current or prior year. All audit fees were borne by the Parent entity in the current and prior year. Total group audit fees for 2019 were £335k (2018: £265k) and this includes audit fees relating to the Company.

7. *Company employees and key management, including directors*

The Company has no employees (2018: none). All services are provided by employees of the Parent, for which a management recharge is made, as disclosed in note 19.

Directors' remuneration

The Directors' emoluments for I Mansfield, J S Mycroft and T Denman were paid by the Parent for their services across both entities. It is not practicable to allocate their respective remuneration across the different group entities.

Notes to the financial statements for the year ended 31 December 2019 (continued)

8. Income tax expense

	2019 £'000	2018 £'000
Current tax:		
United Kingdom corporation tax	2,478	2,246
Adjustments in respect of prior years	(209)	(3)
Deferred tax:		
Deferred tax (credit)/charge for year	(18)	39
Adjustments in respect of prior years	(26)	-
Total tax expense	**2,225**	**2,282**

The actual tax expense for the year differs from that calculated using the standard rate of corporation tax in the UK. The differences are explained below.

	2019 £'000	2018 £'000
Profit before tax	**13,046**	**11,915**
Profit before tax multiplied by the rate of corporation tax of 19.00% (2018: 19.00%)	2,478	2,264
Adjustments in respect of prior years	(235)	(3)
Other	(18)	21
Total tax expense	**2,225**	**2,282**

The statutory rate of corporation tax is 19.0%. The statutory rate of corporation tax will be reduced to 17.0% from April 2020.

Notes to the financial statements for the year ended 31 December 2019 (continued)

9. Property, plant and equipment

2019	Right of use asset £'000	Total £'000
Cost		
At 1 January 2019	-	-
Right of use asset recognised upon adoption of IFRS 16	204	204
At 31 December 2019	**204**	**204**
Depreciation		
At 1 January 2019		-
Charge	123	123
At 31 December 2019	**123**	**123**
Net book value		
At 31 December 2019	**81**	**81**

2018	IT software £'000	Land and buildings £'000	Equipment and vehicles £'000	Total £'000
Cost				
At 1 January 2018	817	83	6,693	7,593
Disposals	(817)	(83)	(6,693)	(7,593)
At 31 December 2018	-	-	-	-
Depreciation				
At 1 January 2018	817	83	6,693	7,593
Disposals	(817)	(83)	(6,693)	(7,593)
At 31 December 2018	-	-	-	-
Net book value				
At 31 December 2018	-	-	-	-

Notes to the financial statements for the year ended 31 December 2019 (continued)

10. Loans and receivables

An analysis of loans and receivables based on contractual payments is as follows:

	2019 £'000	2018 £'000
Customer loans	179,793	236,205
Less: impairment allowance	(6,537)	(8,935)
Net customer loans	**173,256**	**227,270**
Unamortised loan origination costs	5,144	7,694
Accrued interest	942	1,237
	179,342	**236,201**
Other prepayments and accrued income	138	147
	179,480	**236,348**

Reconciliation of movement in impairment allowance

	2019 £'000	2018 £'000
Opening balance at 1 January	**8,935**	**8,787**
Settled loans	(957)	(1,062)
Changes in credit quality	(329)	(1,879)
Changes in model assumptions	(1,112)	3,089
Closing balance at 31 December	**6,537**	**8,935**
Balance sheet impact	(2,398)	148
(Recoveries)/additional write-offs	(1,318)	73
Income statement impact	(3,716)	221

The Company made a recovery of £1,318k through sale of an unsecured portfolio of loans to a third party during the year.

PD Band	2019 Sum of ECL £'000	2019 Coverage %	2018 Sum of ECL £'000	2018 Coverage %
< 0.11%	-	-	-	-
0.11% - 0.17%	-	-	-	-
0.17% - 0.25%	-	-	5	0.1
0.25% - 0.41%	-	-	-	-
0.41% - 0.60%	-	-	40	0.1
0.60% - 0.88%	31	0.1	103	0.2
0.88% - 1.49%	62	0.2	277	0.7
1.49% - 2.96%	334	1.2	835	2.3
2.96% - 6.84%	665	6.9	1,326	9.6
> 6.84%	5,445	19.9	6,349	19.1
Total	**6,537**		**8,935**	

Notes to the financial statements for the year ended 31 December 2019 (continued)

10. Loans and receivables (continued)

Below is a reconciliation of the movement in impairment allowance by stage:

	Stage 1 12-month ECL £'000	Stage 2 Lifetime ECL £'000	Stage 3 Lifetime ECL £'000	Total £'000
Loss allowance as at 1 January 2019	**229**	**5,285**	**3,421**	**8,935**
Transfers:				
Stage 1 Transfers	(3)	-	-	(3)
Stage 2 Transfers	-	110	-	110
Stage 3 Transfers	-	-	(191)	(191)
Settled loans	(33)	(408)	(516)	(957)
Changes in credit quality	(13)	(232)	-	(244)
Changes in model assumptions	(4)	(934)	(174)	(1,113)
Loss allowance at 31 December 2019	**176**	**3,822**	**2,539**	**6,537**

	Stage 1 12-month ECL £'000	Stage 2 Lifetime ECL £'000	Stage 3 Lifetime ECL £'000	Total £'000
Loss allowance as at 1 January 2018	**341**	**4,218**	**4,228**	**8,787**
Transfers:				
Stage 1 Transfers	5	-	-	5
Stage 2 Transfers	-	(137)	-	(137)
Stage 3 Transfers	-	-	(270)	(270)
Settled loans	(51)	(313)	(698)	(1,062)
Changes in credit quality	(67)	(752)	(658)	(1,477)
Changes in model assumptions	1	2,269	819	3,089
Loss allowance at 31 December 2018	**229**	**5,285**	**3,421**	**8,935**

Notes to the financial statements for the year ended 31 December 2019 (continued)

Below is a reconciliation of the movement in loan balance by stage:

	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Loan balance as at 1 January 2019	**180,485**	**44,227**	**13,147**	**237,589**
Transfers:				
Stage 1 Transfers	1,184	-		1,184
Stage 2 Transfers	-	(2,625)		(2,625)
Stage 3 Transfers	-	-	(358)	(358)
Settled loans	(30,983)	(4,515)	(2,057)	(37,555)
Loan Repayments	(14,877)	(2,200)	(555)	(17,362)
Loan balance at 31 December 2019	**135,809**	**34,887**	**10,177**	**180,873**

	Stage 1 £'000	Stage 2 £'000	Stage 3 £'000	Total £'000
Loan balance as at 1 January 2018	**243,655**	**52,954**	**17,001**	**313,609**
Transfers:				
Stage 1 Transfers	(739)			(739)
Stage 2 Transfers		(1,271)		(1,271)
Stage 3 Transfers			(300)	(300)
Settled loans	(44,718)	(5,065)	(2,715)	(52,499)
Loan Repayments	(17,983)	(2,391)	(838)	(21,212)
Loan balance at 31 December 2018	**180,485**	**44,227**	**13,147**	**237,589**

The split of loans between stages 1, 2 and 3 is as follows:

Stage	2019 %	2018 %
1	77	77
2	19	18
3	4	5

The split of the loans within stage 2 by staging reason is as follows:

Staging reason	2019 %	2018 %
PD grade deterioration	74	79
30-60 days past due	26	21

Notes to the financial statements for the year ended 31 December 2019 (continued)

11. Trade and other payables

An analysis of trade and other payables in less than one year is as follows:

	2019 £'000	2018 £'000
Accruals and deferred income	734	975
Sundry creditors	643	760
	1,377	**1,735**

Sundry creditors includes £341k in respect of the lease liability following the adoption of IFRS 16 from 1 January 2019.

12. Regulatory provisions

	2019 £'000	2018 £'000
At 1 January	**3,285**	**3,820**
Utilisation	(590)	(535)
At 31 December	**2,695**	**3,285**

Regulatory provisions have been made in respect of various customer claims, including claims in relation to previous sales of payment protection insurance. Information on the approach to estimating the potential liability is set out in note 2.

13. Financial liabilities

An analysis of the Company's borrowings is as follows:

	2019 £'000	2018 £'000
Current:		
Bank overdrafts	348	287
Non-current :		
Intercompany loans (see note 19)	68,493	135,181

All loans are with the Parent, of which the Company is a subsidiary. Amounts due to the Parent are unsecured and obligations have no fixed repayment date.

Notes to the financial statements for the year ended 31 December 2019 (continued)

14. Deferred tax

The components and movements on the deferred tax account during the year were as follows:

	1 January 2019 £'000	Income Statement £'000	Directly through Equity £'000	31 December 2019 £'000
Assets				
Depreciation in excess of capital allowances	170	26	-	196
Liabilities				
IFRS 9 transitional adjustment	(168)	18	-	(150)
Total	**2**	**44**	**-**	**46**

	1 January 2018 £'000	Income Statement £'000	Directly through Equity £'000	31 December 2018 £'000
Assets				
Depreciation in excess of capital allowances	209	(39)	-	170
Liabilities				
IFRS 9 transitional adjustment	-	-	(168)	(168)
Total	**209**	**(39)**	**(168)**	**2**

The rate of corporation tax for the 2019 financial year was 19% and the rate from 1 April 2020 will be 17%. The impact of this change in rate has been assessed and will not have a material impact on the Company's deferred tax position.

15. Called up share capital

	2019 £'000	2018 £'000
Authorised, allotted and fully paid		
100,000 ordinary shares of £1	100	100

16. Financial risk management

The main financial risks that the Company is exposed to, and its management policy with respect to those risks, are as follows:

- *Interest rate risk:* the possibility that changes in interest rates will result in higher financing costs and/or reduced income from the Company's interest-bearing financial assets and liabilities. Interest rate risk is an inherent trading risk which is actively monitored by the Board.
- *Credit risk:* the risk that counterparties to the Company's financial assets may default. A range of policies and practices is employed to mitigate credit risk – the most common is the taking of security for funds advanced.

Notes to the financial statements
for the year ended 31 December 2019 (continued)

16. Financial risk management (continued)

- *Liquidity risk:* the risk that the Company's cash and committed facilities may be insufficient to meet debts as they fall due. The Company maintains a mixture of committed facilities, including primarily financial support from the Parent, Principality Building Society, that are designed to ensure the Company has sufficient available funds for operations.

The Company's Directors are required to follow the requirements of the Principality Building Society risk management policies, which include specific guidelines on interest rate and credit risks, and advice on the use of financial instruments to manage them.

The risk management policy is in line with the Parent entity – Principality Building Society. Refer to the risk management note in the Society's annual accounts which will be published on the Society's website (http://www.principality.co.uk/).

Maturity of financial instruments

Financial liabilities	**2019 £'000**	**2018 £'000**
In one year or less	348	287
In more than one year but less than two years	-	-
In more than two years but less than five years	68,493	135,181
	68,841	**135,468**

The Company's exposure to interest changes at 31 December 2019 was as follows:

	1 year £'000	**1-5 years £'000**	**Total £'000**
Financial assets			
Loans and receivables	179,342	-	179,342
Financial liabilities			
Borrowings	68,493	-	68,493

The Company's exposure to interest changes at 31 December 2018 was as follows:

	1 year £'000	**1-5 years £'000**	**Total £'000**
Financial assets			
Loans and receivables	236,201	-	**236,201**
Financial liabilities			
Borrowings	135,181	-	**135,181**

Notes to the financial statements for the year ended 31 December 2019 (continued)

17. Contingencies and commitments

Operating lease commitments payable

The future aggregate minimum lease payments under non-cancellable operating leases fall due as follows:

	2019 £'000	2018 £'000
Less than one year	-	541
Later than one year but not later than five years	-	332
Total	**-**	**873**

Lease commitments are now within the lease liability as disclosed in note 11.

Capital and other commitments

There were no capital commitments at 31 December 2019 (2018: none).

18. Events after the balance sheet date

There are no post-balance sheet events.

19. Related party transactions

The definition of related parties includes the Parent, as well as the Company's key management which includes its Directors. There were no such transactions with key management. Particulars of transactions, and the balances outstanding at the year-end (note 13), are disclosed in the tables below:

	2019 Parent company £'000	2018 Parent company £'000
Funding from parent company		
Balance at start of year	135,181	218,761
Interest payable on funding	5,650	7,081
Decrease in funding levels	(72,338)	(90,661)
Balance at end of year	**68,493**	**135,181**

In addition to interest charges, the Company paid £312k (2018: £1,256k) of management recharges to the Parent, which include charges for the provision of services by employees of the Parent.

Notes to the financial statements for the year ended 31 December 2019 (continued)

20. Financial instruments disclosures

a) Categories of financial instruments

Financial assets and liabilities are measured on an ongoing basis either at fair value or at amortised cost.

The accounting policies note describes how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The following tables analyse the financial assets and liabilities in the statement of financial position by the class of financial instrument to which they are assigned, and by the measurement basis:

Financial assets	**2019 £'000**	**2018 £'000**
Loans and receivables	179,342	236,201
The following assets are held at fair value through profit and loss:		
Deferred sale consideration	15	49

b) Carrying values and fair values

The table below compares carrying values and fair values of the Company's financial instruments by category.

The majority of the financial assets and financial liabilities are held at variable rate. The Company loans have been calculated by discounting future cash flows using the effective interest rate associated with each loan. A deduction for incurred losses rather than expected losses has been included.

Carrying Value	**2019 £'000**	**2018 £'000**
Loans and advances to customers	179,342	236,201

Fair Value	**2019 £'000**	**2018 £'000**
Loans and advances to customers	180,735	239,002
Deferred sale consideration	15	49

c) Credit risk

For financial assets recognised on the statement of financial position, the exposure to credit risk equals their carrying amount. For loan commitments and guarantees, the exposure to credit risk is the full amount committed.

	2019 £'000	**2018 £'000**
Financial assets		
Loans and advances to customers	179,342	236,201
Deferred sale consideration	15	49
	179,357	**236,250**

Notes to the financial statements for the year ended 31 December 2019 (continued)

20. Financial instruments disclosures (continued)

The table below provides further information on the Company's loans secured on residential property by payment due status:

	2019 £'000	%	2018 £'000	%
Current and up to date	162,571	89.8	214,100	90.7
Past due up to six months	13,699	7.6	16,512	7.0
Past due over six months	4,603	2.6	5,515	2.3
	180,873	**100.0**	**236,127**	**100.0**

An impairment provision of £6.5m (2018: £8.9m) has been provided for the anticipated losses on the above assets.

The average loan to original value (LTV) in respect of the Company's loans secured on residential property is 64% (2018: 64%). Further LTV information based on original security valuation is shown below:

	2019 %	2018 %
0 - 50%	19	22
50% - 75%	54	51
75% - 85%	15	15
More than 85%	12	12
	100	**100**

The average balance to current value (BTV) in respect of the Company's loans secured on residential property is 54% (2018: 53%). Further LTV information based on current security valuation is shown below:

	2019 %	2018 %
0 - 50%	48	42
50% - 75%	44	48
75% - 85%	5	7
85% - 100%	3	3
More than 100%	-	-
	100	**100**

Non-arrears customers are indexed using Nationwide HPI and all non performing accounts are valued using the Hometrack desktop valuation model.

d) Market risk

The sole source of market risk is interest rate risk, as outlined below.

Notes to the financial statements for the year ended 31 December 2019 (continued)

20. Financial instruments disclosures (continued)

e) Interest rate risk

The Company's exposure to interest rate risk is managed through close monitoring of interest rates on its loan products.

The Company is funded by a variable interest rate loan from the Parent, details of which are included in notes 13 and 16. The exposure to variable rate funding is managed through the close monitoring of variable interest rates on the Company's loan products and the rate on the loan to the Company from its Parent.

Funding is carried out at a Group level considering both maturity and interest type. The Company sees the interest rate risk to be immaterial.

The Company holds collateral against loans and advances to residential customers in the form of mortgage interests over property. Repossessed properties are made available for sale at the time of the repossession in accordance with statutory guidelines with proceeds used to reduce or repay the outstanding loan. The Company has a statutory duty to obtain the best reasonable price and to sell as soon as it reasonably can.

21. Provisions and contingent liabilities

Regulatory provision

Provisions have been made in respect of historic customers claims (note 12). At 31 December 2019, provisions of £2.7m were held (2018: £3.3m).

Although the provision balance is expected to be sufficient to meet any remaining obligations, a significant degree of uncertainty remains with regard to the ultimate cost of settling customer claims. The provision will continue to be monitored and customer trends and behaviour analysed in order ensure the provision remains appropriate.

22. Ultimate holding party

Principality Building Society is ultimate controlling party and the Parent of the smallest and largest Company of which Nemo is a member and for which Group financial statements are drawn up. Copies of the Principality Building Society Group's annual report will be published on the Society's website (http://www.principality.co.uk).