

Registered number: 05924768

**Eurosail 2006-3NC plc**

**Reports and audited financial statements  
for the year ended 30 November 2018**



## **Eurosail 2006-3NC plc**

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## **Eurosail 2006-3NC plc**

### **Company information**

<b>Directors</b>	Wilmington Trust SP Services (London) Limited D J Wynne
<b>Company secretary</b>	Wilmington Trust SP Services (London) Limited
<b>Registered office</b>	Third Floor, 1 King's Arms Yard London EC2R 7AF
<b>Independent auditor</b>	KPMG LLP One Snowhill, Snow Hill Queensway Birmingham B4 6GH
<b>Registered number</b>	05924768
<b>Note trustee</b>	BNY Mellon Corporate Trustee Services Limited One Canada Square London E14 5AL

# Eurosail 2006-3NC plc

## Strategic report for the year ended 30 November 2018

The directors present their strategic report on Eurosail 2006-3NC plc (the "Company") for the year ended 30 November 2018.

### Introduction

The Company, a public company limited by shares was incorporated on 5 September 2006 in England, United Kingdom and is registered in England and Wales under the Companies Act 2006. The Company is a special purpose vehicle which acts as an issuer in a residential mortgage backed securitisation transaction. The principal activity of the Company is the investment in mortgage loans secured by first and second charges over properties within the United Kingdom.

In November 2006, the Company purchased £505,250,000 of mortgage assets from Southern Pacific Mortgage Limited. Further consideration in the form of deferred consideration may be payable to Southern Pacific Mortgage Limited dependent on the future performance of the mortgages. As a consequence of the transfer of the mortgages not qualifying for derecognition, the mortgages have continued to be recognised as loans to originator as detailed in note 2.6 of the financial statements. To facilitate the purchase, the Company issued a series of loan notes in November 2006. These loan notes are issued on Euronext Dublin (formerly the Irish Stock Exchange) and are due in 2044.

The mortgage servicing, cash bond administration and accounting services are provided by Acenden Limited, an external party.

### Business review

The results for the year ended 30 November 2018 are set out on page 17. Both the level of business during the year and the financial position of the Company at the end of the year were satisfactory given the nature of the Company and its limited recourse liability.

At the year end, the loans to originator balance after the effective interest rate adjustment, specific provisions and unamortised discounts and premiums on acquisition was £100,774,000 (2017: £109,663,000) on 1,412 mortgages. The estimated weighted average remaining life of the mortgage assets is 5.3 years (2017: 5.4 years).

After considering property values, anticipated bad debts and future income associated with the mortgage assets underlying the loans to originator, over and above the principal figure shown above, the directors consider the mortgage assets together with the other related assets of the Company such as cash, to be adequate collateral against the mortgage backed loan notes in issue. The weighted average funding costs are 0.48% (2017: 0.45%) above LIBOR and the weighted average interest on mortgage assets is 4.49% (2017: 3.97%).

At year end the Company held the following principal balances of mortgage assets underlying the loans to originator.

	2018 Principal balance £'000	2018 Number of loans	2017 Principal balance £'000	2017 Number of loans
First charge mortgages	86,166	1,031	95,512	1,113
Second charge mortgages	8,835	381	10,230	425
	<u>95,001</u>	<u>1,412</u>	<u>105,742</u>	<u>1,538</u>

These mortgages provide security against loan notes in issue totalling £35,512,000 and €91,739,000 (2017: £40,495,000 and €99,691,000) as at the year end excluding accrued interest.

## Eurosail 2006-3NC plc

### Strategic report for the year ended 30 November 2018

The directors have concluded that the Company will continue as a going concern and set out the basis for this conclusion in the going concern section of the directors' report.

#### Key performance indicators

The key performance indicator of the Company is the quarterly arrears profile of the mortgage assets underlying the loans to originator:

	Mar-18	Jun-18	Sep-18	Dec-18
Delinquencies days	%	%	%	%
Current	68.42	68.46	68.63	67.79
>30<=60	5.99	6.76	6.67	6.90
>60<=90	4.86	3.96	4.56	5.98
>90<=120	3.35	3.78	3.10	3.03
>120	17.38	17.04	17.04	16.30
Total	100.00	100.00	100.00	100.00

The value of mortgages in repossession at the year end is £771,000 (2017: £570,000).

A monthly accrual is made in the statement of comprehensive income for deferred consideration that will ultimately become payable. Under the terms of the waterfall payments, any deferred consideration would only be paid when there are sufficient revenue funds available and all other liabilities in the waterfall have been satisfied. Cash flow projections have been prepared to determine the extent to which deferred consideration will be payable. Based on these projections, the directors have determined that £13,113,000 (2017: £11,167,000) consideration was payable at the year end.

#### Principal risks and uncertainties

##### Financial instrument risk

The financial instruments held by the Company comprise mortgage assets underlying the loans to originator, borrowings, cash and various other items (such as other debtors and other creditors) that arise directly from its operations.

The Company also enters into derivative transactions where necessary to manage its interest rate and currency risk. Details of any derivatives held by the Company are disclosed in note 18.

It is, and has been throughout the year under review, the Company's policy that no trading in financial instruments shall be undertaken.

The main risks arising from the Company's financial instruments are credit risk, liquidity risk, foreign exchange risk, interest rate risk and operational risk. The directors review and agree policies for managing each of these risks and they are summarised below.

##### (a) Credit risk

The underlying mortgages are classified as loans to originator, this means that in the first instance the recovery of the debt is against the originating company Southern Pacific Mortgage Limited. The mortgages are fully secured against the loan and therefore ring fenced from other creditors in the originating company and the originating company is bound under the contractual terms to pay across the cash flows from the underlying loans, therefore credit risk is assessed as being against the underlying mortgages.

## **Eurosail 2006-3NC plc**

### **Strategic report for the year ended 30 November 2018**

Credit risk is the risk that borrowers will not be able to meet their obligations as they fall due. All mortgage assets underlying the loans to originator were required to adhere to specific lending criteria. The ongoing credit risk of the mortgage portfolio (and particularly in respect of accounts in arrears) is closely monitored through an assessment of each customer and the prevailing macroeconomic environment. Probability of default of the customer and the loss given default is calculated and impairment provisions raised where necessary. The mortgage portfolio is recognised as collateralised non-recourse mortgage loans as explained in note 2. In addition, where derivatives are held by the Company, there is a credit risk associated with the ability of the swap counterparty to meeting its obligations under the swap agreement. In some instances, this may be mitigated by the payment of cash collateral to the Company. Details of any cash collateral held by the Company are included in note 18.

The directors continue to closely monitor the economic landscape to ensure the Company is best placed to respond to any pressures that may impact portfolio performance and proactively consider strategies to mitigate any adverse portfolio impact should these pressures occur.

#### **(b) Liquidity risk**

The Company's policy is to manage liquidity risk by matching the timing of the cash receipts from mortgage assets underlying the loans to originator with those of the cash payments due on the loan notes. In addition the Company holds a minimum cash balance to manage short term liquidity requirements.

#### **(c) Foreign exchange risk**

Foreign exchange risk exists where the loan notes are denominated in a currency which is different to the underlying Sterling mortgage loans. Where this exists, the Company minimises its exposure to foreign currency risk by ensuring that the currency characteristic of its assets and liabilities are similar. Where this is not possible the Company has used derivative financial instruments to mitigate any foreign exchange risk. Details of foreign exchange exposures and any related derivatives held by the Company are disclosed in note 18.

#### **(d) Interest rate risk**

Interest rate risk exists where assets and liabilities have interest rates set under different bases or which reset at different times. The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of its assets and liabilities are similar. Where this is not possible the Company has used derivative financial instruments to mitigate any residual interest rate risk. Details of interest rate risk exposures and any related derivatives held by the Company are disclosed in note 18.

#### **(e) Operational risk**

Operational risk is defined as any instance where there is potential or actual impact to the Company resulting from inadequate or failed internal processes, people, systems, or from external events. The impacts can be financial as well as non-financial such as customer detriment, reputational or regulatory consequences.

The Company operates under a controls and governance framework provided by the servicer of the mortgage assets underlying the loans to originator. This includes regulatory and compliance functions and internal audit. The business is covered by the servicer's business continuity management capability.

## **Eurosail 2006-3NC plc**

### **Strategic report for the year ended 30 November 2018**

#### **Future business developments and strategy**

The directors expect the business will continue in its principal activities described above for the foreseeable future and will ensure that customers continue to be serviced on a business as usual basis.

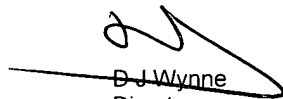
The business is subject to a number of risks under the principal risks and uncertainties section, which could adversely affect the business in future years, and the directors will continue to monitor and manage those risks.

The continued lack of clarity on Brexit, or more specifically the ongoing relationship of the UK with the EU after 29 March 2019, results in a high degree of uncertainty in the financial markets. This could lead to a change in the behavioural characteristics of the mortgage assets underlying the loans to originator, which may result in an increase in impairment losses and/or a differing unwind on the Company's EIR adjustments. To the extent that the impact of this unprecedented situation can be predicted, changes in these behavioural characteristics has been reflected in the cash flow models which underpin the impairment loss and EIR adjustments as at 30 November 2018.

However, due to the limited recourse nature of the loan notes issued by the Company, any impact of this uncertainty on the results of the Company will not impact on its ability to continue to operate as a going concern.

To date, there have been no matters that warrant adjustment to the Company's financial results as at 30 November 2018 and for the year then ended.

This report was approved by the Board on 27 March 2019 and signed on its behalf by:



D J Wynne  
Director

Date: 27 March 2019

## **Eurosail 2006-3NC plc**

### **Directors' report for the year ended 30 November 2018**

The directors present their report together with the audited financial statements of the Company for the year ended 30 November 2018.

#### **Results and dividends**

The loss for the year, after taxation, amounted to £601,000 (2017: loss of £3,362,000).

The directors do not recommend the payment of a dividend (2017: nil).

#### **Future developments**

An assessment of the Company's future developments is described in the strategic report under the future business developments and strategy section.

#### **Financial instruments**

An assessment of the Company's financial instruments is described in the strategic report under the principal risks and uncertainties section.

#### **Directors**

The directors who held office during the year and up to the date of the approval of the financial statements, except as noted, are given below:

Wilmington Trust SP Services (London) Limited  
D J Wynne

None of the above directors have any interest in the shares of the Company. There are no directors' interests requiring disclosure under the Companies Act 2006.

#### **Company secretary**

Wilmington Trust SP Services (London) Limited continued to act as company secretary for the year ended 30 November 2018 and up to the date of signing the financial statements.

#### **Going concern**

The Company has reported an operating loss for the current year and is in a net liability position as at 30 November 2018.

It is the intention of the directors of the Company to continue operations until such a time as the amount due from mortgage assets underlying the loans to originator have been fully realised. Forecasts indicate that the Company will have adequate cash to enable it to meet its obligations within the next 12 months from the date of the approval of these financial statements.

A call option exists over the notes which may be exercised at the sole discretion of the issuer (with the approval of the trustee) once the outstanding mortgage backed loan notes reach 10% of the original issued amount. The threshold has not been satisfied.

Due to the non-recourse nature of the loan notes, any shortfall in the proceeds from the mortgage assets underlying the loans to originator will be a risk to the holders of these notes and accordingly the financial statements have been prepared on a going concern basis.



# **Eurosail 2006-3NC plc**

## **Directors' report for the year ended 30 November 2018**

### **Post balance sheet date events**

To date, there have been no matters that warrant adjustment to the Company's financial results as at 30 November 2018 and for the year then ended.

### **Principal risks and uncertainties**

The business is subject to a number of risks, described in the strategic report under the principal risks and uncertainties section, which could adversely affect the business in future years and the directors will continue to monitor and manage those risks.

### **Fair value**

Note 18 discloses the fair values of the mortgage assets underlying the loans to originator and loan notes. The directors noted that as at 30 November 2018 the respective fair values of the mortgage assets underlying the loans to originator were higher than and loan notes were lower than the carrying values recorded in the statement of financial position.

As no liquid market exists for either the mortgage assets underlying the loans to originator or loan notes, the directors have ascribed an approximate fair value based on an internal discounted cash flow model that is used to value non-securitised mortgage loan receivables. This model takes into account expected prepayment rates, arrears levels, house price movements, level of repossessions, losses and discount rates based on the most recent available information.

### **Corporate governance**

The directors have been charged with governance in accordance with the transaction documents describing the structure and operation of the Company. The governance structure of the Company is such that the key policies have been predetermined at the time of the transaction documents issuance and the operational roles have been assigned to third parties with their roles strictly governed by the transaction documents.

The transaction documents provide for procedures that have been designed for safeguarding assets against unauthorised use or disposition, for maintaining proper accounting records, and for the reliability and usefulness of financial information used within the business or for publication. Such procedures are designed to manage, rather than eliminate the risk of failure to achieve business objectives, whilst enabling them to comply with the regulatory obligations.

Due to the nature of the securities which have been issued on the Euronext Dublin (formerly the Irish Stock Exchange), the directors are satisfied that there is no requirement to publish a corporate governance statement and that the Company is largely exempt from the requirements of the Irish Corporate Governance Annex and the provisions of the UK Corporate Governance Code. do not apply to the Company.

### **Employees**

The Company does not have any employees (2017: none).

### **Issued capital and capital contribution**

Details of the share capital are set out in note 19 to the financial statements. The issued share capital consists of £12,502 comprising 50,000 ordinary shares of £1 each with 2 ordinary shares being fully paid and 49,998 ordinary shares being partly paid.

## **Eurosail 2006-3NC plc**

### **Directors' report for the year ended 30 November 2018**

#### **Qualifying third party indemnity provisions**

Qualifying third party indemnity provisions for the benefit of the directors, in accordance with section 234 of the Companies Act 2006, were in force during the period under review and remain force as at the date of approval of the directors' report and financial statements.

#### **Disclosure of information to the auditor**

Each of the persons who are directors at the time when this directors' report is approved has confirmed that:

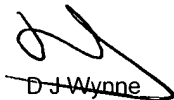
- so far as the director is aware, there is no relevant audit information of which the Company's auditor is unaware, and
- the director has taken all the steps that ought to have been taken to make himself aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of section 418(2) of the Companies Act 2006.

#### **Auditor**

The auditor, KPMG LLP, has indicated its willingness to continue in office and a resolution concerning its re-appointment will be considered at the forthcoming Annual General Meeting.

This report was approved by the Board on 27 March 2019 and signed on its behalf by:



D J Wynne  
Director  
Date: 27 March 2019

## **Eurosail 2006-3NC plc**

### **Statement of directors' responsibilities in respect of the Annual Report, the Strategic Report, the Directors' Report and the Financial Statements**

The directors are responsible for preparing the Annual Report, the Strategic Report, the Directors' 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 they have elected to prepare the financial statements in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice), including FRS 101 Reduced Disclosure Framework.

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 its profit or loss for that period. In preparing the financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable, and prudent;
- state whether applicable UK accounting standards have been followed, subject to any material departures disclosed and explained in the financial statements;
- assess the 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 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 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 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 Company and to prevent and detect fraud and other irregularities.

Under applicable law and regulations, the directors are also responsible for preparing a Strategic Report, Directors' Report, and Corporate Governance Statement that complies with that law and those regulations.

# INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF EUROSAIL 2006-3NC PLC

## 1 Our opinion is unmodified

We have audited the financial statements of Eurosail 2006-3NC plc ("the Company") for the year ended 30 November 2018 which comprise the statement of comprehensive income, statement of financial position, statement of changes in equity, and the related notes, including the accounting policies in note 2.

In our opinion the financial statements:

- give a true and fair view of the state of Company's affairs as at 30 November 2018 and of its loss for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 101 *Reduced Disclosure Framework*; and
- 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 first appointed as auditor by the directors on 9 March 2018. The period of total uninterrupted engagement is for the 2 financial years ended 30 November 2018. We have fulfilled our ethical responsibilities under, and we remain independent of the Company in accordance with, UK ethical requirements including the FRC Ethical Standard as applied to listed public interest entities. No non-audit services prohibited by that standard were provided.

## 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. We summarise below the key audit matters, 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.

Key audit matter	The risk	Our response
<p><b>The impact of uncertainties due to Britain exiting the European Union on our audit</b></p> <p><i>Refer to page 5 (strategic report)</i></p>	<p><b>Unprecedented levels of uncertainty</b></p> <p>All audits assess and challenge the reasonableness of estimates, in particular as described in impairment of loans to originator, interest receivable – effective interest rate adjustment below, related disclosures and the appropriateness of the going concern basis of preparation of the annual accounts. All of these depend on assessments of the future economic environment</p>	<p>We have developed a standardised firm-wide approach to the consideration of the uncertainties arising from Brexit in planning and performing our audits. Our procedures included:</p> <p>— <b>Our Brexit knowledge</b> – We considered the directors' assessment of Brexit-related sources of risk for the Company's business and financial resources compared with our own understanding of the risks. We considered the</p>

and the Company's future prospects and performance. In addition, we are required to consider the other information presented in the Annual Report including the principal risks disclosure and to consider the directors' statement that the annual report and financial statements taken as a whole is fair, balanced and understandable and provides the information necessary for noteholders to assess the Company's position and performance, business model and strategy.

Brexit is one of the most significant economic events for the UK and at the date of this report its effects are subject to unprecedented levels of uncertainty of outcomes, with the full range of possible effects unknown.

directors' plans to take action to mitigate the risks.

- **Sensitivity analysis** – When addressing impairment of loans to originator and interest receivable – effective interest rate adjustment, we compared the directors' sensitivity analysis to our assessment of the full range of reasonably possible scenarios resulting from Brexit uncertainty
- **Assessing transparency** – As well as assessing individual disclosures as part of our procedures on impairment of loans to originator and interest receivable – effective interest rate adjustment we considered all the Brexit related disclosures together, including those in the strategic report, comparing the overall picture against our understanding of the risks.

#### Our results

As reported under impairment of loans to originator and interest receivable – effective interest rate adjustment, we found the resulting estimates and related disclosures of sensitivity and disclosures in relation to going concern to be acceptable. However, no audit should be expected to predict the unknowable factors or all possible future implications for a Company and this is particularly the case in relation to Brexit.

Key audit matter	The risk	Our response
<b>Impairment of loans to originator</b>  <i>Refer to page 23 (accounting policy) and page 31 (financial disclosures).</i>	<p><b>Subjective estimate:</b> The impairment provision relating to the Company's loans to originator requires the directors to make significant judgements and estimates in order to determine incurred losses on those assets.</p> <p>The impairment provision is derived from a model that uses observable data relating to the loans to originator such as adverse changes in payment status of the borrower, or economic conditions that</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>— <b>Controls testing:</b> We performed end to end process walk-throughs to identify the key systems, applications and controls used in the loan impairment process. We tested the relevant general IT and applications controls over key systems used in the loan impairment process.</li> </ul>

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correlate with defaults in the loans to originators. The model also incorporates historical data on similar types of mortgage assets.

As probability of defaults ('PDs') and loss given defaults ('LGDs') are calculated at an individual loan level, the directors assess all impairment provisions on an individual basis.

There is a risk that the impairment provision is not reflective of the incurred losses at the end of the period due to the time that it takes for incurred losses to emerge, changes in customer credit quality or other market factors not sufficiently incorporated into the judgement, such as house prices.

— **Test of details:** Key aspects of our testing involved: developing a point estimate based on the historical credit performance of the Company to evaluate the directors' impairment of loans to originator estimate; and for a sample of specific loans identified based on risk characteristics of current or historical arrears, forbearance and loan type, we evaluated whether they have been adequately provided for.

— **Benchmarking assumptions:** We compared the Company's key assumptions being PD and LGD, against those of comparable securitisation vehicles to assess both the level of impairment provision in comparison to industry norms and the continuing appropriateness of the assumptions used.

— **Sensitivity analysis:** We performed sensitivity analysis over the Company's PDs and LGDs to help us assess the reasonableness of the assumptions used.

— **Assessing transparency:** We evaluated whether the disclosures appropriately reflect and address the uncertainty which exists when determining the impairment of loans to originator. As a part of this, we assessed the sensitivity analysis that is disclosed. In addition, we challenged whether the disclosure of the key judgments and assumptions made was sufficiently clear.

#### **Our results**

We found the impairment on loans to originator recognised and the related disclosures to be acceptable (2017: acceptable).

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Key audit matter	The risk	Our response
<p><b>Interest receivable – effective interest rate adjustment</b></p> <p><i>Refer to page 21 (accounting policy) and page 28 (financial disclosures).</i></p>	<p><b>Subjective estimate:</b> Using management's cash flow modelling tool, fees earned and incurred on loans are recognised using the effective interest rate ('EIR') method that spreads directly attributable expected cash flows over the expected lives of the loans.</p> <p>Management apply judgement in deciding and assessing the expected repayment profiles used to determine the EIR period. This is the most critical element of judgement, informed by past customer behaviour of when loans are repaid. The expected behavioural life has a direct impact on the level of income recognised by the entity.</p> <p>EIR modelling is complex and so open to the possibility that the modelling principles are not in accordance with accounting requirements.</p> <p><b>Data capture:</b> The cash flow modelling tool uses both internal and external data inputs. This includes both current and historic data specific to the Company's mortgage assets, as well as similar mortgage assets, and macroeconomic data.</p> <p>The macroeconomic data incorporates expectations regarding HPI and base rates/LIBOR. Owing to the risk of inaccurate data inputs there is a risk that the cash flow models generated are inaccurate.</p>	<p>Our procedures included:</p> <ul style="list-style-type: none"> <li>— <b>Control testing:</b> We tested controls over management's assessment of, and subsequent approval of, both the updated cash flow model and the resulting EIR adjustments.</li> <li>— <b>Methodology implementation:</b> We compared the model's methodology with the requirements of the relevant accounting standard.</li> <li>— <b>Historical comparison:</b> We have assessed the reasonableness of the cash flow model derived by the directors which models the expected lives of the loan book. This included assessing the historical accuracy of the key cash flow model assumptions, including conditional prepayment rates ('CPR').</li> <li>— <b>Test of details:</b> We tested the accuracy of data inputs from the mortgage system into the effective interest rate model, including outstanding balance and contractual maturity.</li> <li>— <b>Data comparison:</b> We checked both a sample of the internal/external data and the data totals used in the model back to the entities underlying source (e.g. current balance on the mortgage loan system) and external economic guidance. We also agreed the life profile assumptions in the model to the profiles produced by the cash flow modelling tool, and assessed as outlined above.</li> <li>— <b>Independent re-performance:</b> We</li> </ul>

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performed a recalculation of the EIR adjustments recognised in the income statement during the year. This included reconciling to the closing balance sheet positions.

- **Assessing transparency:**  
We evaluated whether the disclosures appropriately reflect and address the level of judgment which exists when determining revenue recognition on the Company's mortgage assets. In addition, we challenged whether the disclosure of the key judgments and assumptions made was sufficiently clear.

**Our results**

We found the resulting revenue recognition to be acceptable (2017: acceptable).

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

Materiality for the Company financial statements as a whole was set at £0.7 million, determined with reference to a benchmark of total assets, of which it represents 0.75% (2017: 0.75% of total assets).

We agreed to report to those charged with governance any corrected or uncorrected identified misstatements exceeding £0.04 million, in addition to other identified misstatements that warranted reporting on qualitative grounds.

**4 We have nothing to report on going concern**

The Directors have prepared the financial statements on the going concern basis as they do not intend to liquidate the Company or to cease its operations, and as they have concluded that the Company's financial position means that this is realistic. They have also concluded that there are no material uncertainties that could have cast significant doubt over its ability to continue as a going concern for at least a year from the date of approval of the financial statements ("the going concern period").

Our responsibility is to conclude on the appropriateness of the Directors' conclusions and, had there been a material uncertainty related to going concern, to make reference to that in this audit report. However, as we cannot predict all future events or conditions and as subsequent events may result in outcomes that are inconsistent with judgements that were reasonable at the time they were made, the absence of reference to a material uncertainty in this auditor's report is not a guarantee that the Company will continue in operation.

In our evaluation of the Directors' conclusions, we considered the inherent risks to the Company's business model, including the impact of Brexit, and analysed how those risks might affect the Company's financial resources or ability to continue operations over the going concern period. We evaluated those risks and concluded that they were not significant enough to require us to perform additional audit procedures.

Based on this work, 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 a year from the date of approval of the financial statements.

We have nothing to report in these respects, and we did not identify going concern as a key audit matter.

#### **5 We have nothing to report on the other information in the Annual Report**

The directors are responsible for the other information presented in the Annual Report together with the financial statements. Our opinion on the financial statements does not cover the other information and, accordingly, we do not express an audit opinion or, except as explicitly stated below, any form of assurance conclusion thereon.

Our responsibility is to read the other information 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 the other information.

##### ***Strategic report and directors' report***

Based solely on our work on the other information:

- we have not identified material misstatements in the strategic report and the directors' report;
- in our opinion the information given in those reports 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 Company, 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 these respects.

#### **7 Respective responsibilities**

##### ***Directors' responsibilities***

As explained more fully in their statement set out on page 9, 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 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 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](http://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 annual accounts from our general commercial and sector experience, through discussion with the directors (as required by auditing standards), and from inspection of the Group's

regulatory correspondence and discussed with the directors the policies and procedures regarding compliance with laws and regulations. We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit.

Through these procedures we became aware of actual or suspected non-compliance and considered the effect as part of our procedures on the related financial statement items. The actual or suspected non-compliance was not sufficiently significant to our audit to result in our response being identified as a key audit matter.

The potential effect of these laws and regulations on the financial statements varies considerably.

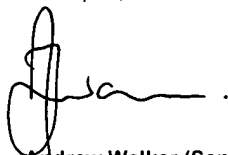
The company is subject to laws and regulations that directly affect the financial statements including financial reporting legislation (including related companies legislation), distributable profits legislation, and taxation legislation and we assessed the extent of compliance with these laws and regulations as part of our procedures on the related financial statement items.

Whilst the company is subject to many other laws and regulations, we did not identify any others where the consequences of non-compliance alone could have a material effect on amounts or disclosures in the financial statements.

Owing to the inherent limitations of an audit, there is an unavoidable risk that we may not have detected some material misstatements in the financial statements, even though we have properly planned and performed our audit in accordance with auditing standards. For example, the further removed non-compliance with laws and regulations (irregularities) is from the events and transactions reflected in the financial statements, the less likely the inherently limited procedures required by auditing standards would identify it. In addition, as with any audit, there remained a higher risk of non-detection of irregularities, as these may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal controls. We are not responsible for preventing non-compliance and cannot be expected to detect non-compliance with all laws and regulations.

#### **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.



**Andrew Walker (Senior Statutory Auditor)**  
**for and on behalf of KPMG LLP, Statutory Auditor**  
*Chartered Accountants*  
One Snowhill,  
Snow Hill Queensway  
Birmingham  
B4 6GH

28 March 2019

## Eurosail 2006-3NC plc

### Statement of comprehensive income for the year ended 30 November 2018

	Note	2018 £'000	2017 £'000
Interest receivable and similar income	4	6,240	2,925
Interest payable and similar expenses	5	(753)	(540)
<b>Net interest receivable</b>		<u>5,487</u>	<u>2,385</u>
Operating expenses		(5,025)	(5,570)
Other operating income	6	11	5
		<u>473</u>	<u>(3,180)</u>
Net fair value (loss)/gain on derivatives		(703)	2,808
Unrealised exchange loss on retranslation of loan notes		(508)	(3,789)
<b>Loss before taxation</b>	7	<u>(738)</u>	<u>(4,161)</u>
Tax credit on loss	8	137	799
<b>Loss and total comprehensive expense for the financial year</b>		<u>(601)</u>	<u>(3,362)</u>

All amounts relate to continuing operations.

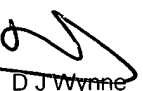
There were no items of other comprehensive income for 2018 or 2017 and therefore no separate statement of other comprehensive income has been presented.

The notes on pages 20 to 44 are an integral part of these financial statements.

**Eurosail 2006-3NC plc****Statement of financial position  
as at 30 November 2018**

	<b>Note</b>	<b>2018 £'000</b>	<b>2017 £'000</b>
<b>Non-current assets</b>			
Debtors: amounts falling due after more than one year	11	88,420	96,974
<b>Current assets</b>			
Deferred tax assets	17	439	296
Debtors: amounts falling due within one year	12	12,386	12,720
Derivative financial instruments	18	20,825	22,690
Cash and cash equivalents	14	11,488	13,568
<b>Total current assets</b>		<u>45,138</u>	<u>49,274</u>
<b>Current liabilities</b>			
Creditors: amounts falling due within one year	15	(18,627)	(19,222)
<b>Total assets less current liabilities</b>		<u>114,931</u>	<u>127,026</u>
<b>Non-current liabilities</b>			
Creditors: amounts falling due after more than one year	16	(116,736)	(128,230)
<b>Net liabilities</b>		<u>(1,805)</u>	<u>(1,204)</u>
<b>Capital and reserves</b>			
Called up share capital	19	13	13
Accumulated losses		(1,818)	(1,217)
<b>Total deficit</b>		<u>(1,805)</u>	<u>(1,204)</u>

These financial statements were approved and authorised for issue by the Board on 27 March 2019 and were signed on its behalf by:

  
D J Wynne  
Director  
Date: 27 March 2019

The notes on pages 20 to 44 are an integral part of these financial statements.

## Eurosail 2006-3NC plc

### Statement of changes in equity for the year ended 30 November 2018

	Called up share capital	Accumulated losses	Total deficit
	£'000	£'000	£'000
Balance at 1 December 2016	13	2,145	2,158
Loss for the financial year	-	(3,362)	(3,362)
<b>Balance at 30 November 2017</b>	<b>13</b>	<b>(1,217)</b>	<b>(1,204)</b>
Balance at 1 December 2017	13	(1,217)	(1,204)
Loss for the financial year	-	(601)	(601)
<b>Balance at 30 November 2018</b>	<b>13</b>	<b>(1,818)</b>	<b>(1,805)</b>

The notes on pages 20 to 44 are an integral part of these financial statements.

# **Eurosail 2006-3NC plc**

## **Notes to the financial statements for the year ended 30 November 2018**

### **1 General information**

The principal activity of the Company is the investment in mortgage loans secured by first and second charges over properties within the United Kingdom.

The Company is a public limited company and was incorporated on 5 September 2006 and is domiciled in England, United Kingdom. Its principal place of business is its registered office located at Wilmington Trust SP Services (London) Limited, Third Floor, 1 King's Arms Yard, London, EC2R 7AF.

### **2 Significant accounting policies**

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Company's financial statements:

#### **2.1. Basis of preparation and statement of compliance with FRS 101**

The financial statements have been prepared in accordance with Financial Reporting Standard 101 'Reduced Disclosure Framework' (FRS 101). The financial statements have been prepared on a going concern basis, under the historical cost convention as modified by the financial assets and liabilities measured at fair value through profit or loss, and in accordance with the Companies Act 2006. The disclosure exemptions adopted by the Company in accordance with FRS 101 are as follows:

- The requirements of IAS 7 Statement of Cash Flows;
- The requirements of paragraphs 10(d), 10(f), 16, 38(c)-(d), 40(a)-(d), 111 and 134-136 of IAS 1 Presentation of Financial Statements;
- The requirements of paragraphs 30 and 31 of IAS 8 Accounting Policies, Changes in Accounting Estimates and Errors; and
- The Company has taken advantage of the exemptions conferred by FRS 101: 8 (j) & (k) "Related party disclosures", the requirements of paragraph 17 and 18A of IAS 24 Related Party Disclosures, and transactions with other wholly owned group companies are not disclosed separately.

The preparation of financial statements in conformity with FRS 101 requires the use of certain significant accounting estimates and assumptions. It also requires management to exercise its judgement in the process of applying the Company's accounting policies. The areas involving a higher degree of judgement or complexity, or areas where assumptions and estimates are significant to the financial statements, are disclosed in note 3.

#### **2.1.1 Going concern**

It is the intention of the directors to continue operations until such a time as the amount due from the mortgage assets underlying the loans to originator have been fully realised. Forecasts indicate that the Company will have adequate cash to enable it to meet its obligations within the next 12 months from the date of the approval of these financial statements.

A call option exists over the notes which may be exercised at the sole discretion of the issuer (with the approval of the trustee) once the outstanding mortgage backed loan notes reach 10% of the original issued amount. The threshold has not been satisfied.

Due to the non-recourse nature of the loan notes, any shortfall in the proceeds from the mortgage assets underlying the loans to originator will be a risk to the holders of these notes and accordingly the financial statements have been prepared on a going concern basis.

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **2.2. Interest recognition**

Interest income on mortgage assets underlying the loans to originator, together with the interest expense on the mortgage backed loan notes, is recognised in the statement of comprehensive income on an Effective Interest Rate ("EIR") basis. The EIR basis recognises revenue and expenses equivalent to the rate that effectively discounts estimated future cash flows throughout the expected life to the net carrying value of the mortgage assets underlying the loans to originator or mortgage backed loan notes.

#### **2.3. Current and deferred tax**

The tax expense for the year comprises current and deferred tax. Tax is recognised in the statement of comprehensive income, except to the extent that it relates to items recognised in other comprehensive income or directly in total equity. In this case the tax is also recognised in other comprehensive income or directly in total equity, respectively.

The current income tax expense is calculated on the basis of the tax laws enacted or substantively enacted at the statement of financial position date in the countries where the Company operates and generates taxable income. Management periodically evaluates positions taken in tax returns in respect to situations in which applicable tax regulation is subject to interpretation. It establishes provisions where appropriate on the basis of amounts expected to be paid to the tax authorities.

Deferred income tax is recognised on deductible temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantively enacted by the statement of financial position date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred income tax assets are recognised only to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the same taxable entity or different taxable entities where there is an intention to settle the balances on a net basis.

#### **2.4. Foreign currencies**

The financial statements are presented in pounds Sterling (£), which is the functional and presentation currency of the Company. All amounts in these financial statements have been rounded to the nearest thousand, unless otherwise indicated.

Transactions in foreign currency are initially converted to Sterling at the rate ruling at the date of the transaction. Monetary assets and liabilities denominated in foreign currencies are translated into Sterling at rates of exchange prevailing at the reporting date. All differences on exchange are taken to the statement of comprehensive income.

#### **2.5. Loan notes**

Loan notes are initially recognised at fair value less attributable transaction costs. Subsequent to initial recognition, the loan notes are measured at amortised cost with any difference between cost and redemption value being recognised in the statement of comprehensive income over the period of the borrowings on an EIR basis.

The repayment of the loan notes is dependent on principal and interest collections on the mortgage loans.

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **2.6. Financial instruments**

##### **Initial recognition**

The Company recognises financial assets and liabilities when it becomes a party to the terms of the contract.

Purchases or sales of financial assets that require delivery of assets within a time frame established by regulation or convention in the marketplace (regular way trades) are recognised on the trade date, i.e., the date on which the Company commits to purchase or sell the asset.

##### **Classification and measurement**

Financial assets and liabilities are initially classified as financial assets or liabilities at fair value through profit or loss, loans and receivables and available for sale financial assets.

All financial assets are recognised initially at fair value plus directly attributable costs for those not at fair value through profit and loss.

Financial liabilities are recognised initially at fair value and in the case of loans and borrowings payables, net of directly attributable transaction costs.

The subsequent measurement of financial assets depends on their classification as follows:

##### **Financial assets at fair value through profit or loss**

Financial assets at fair value through profit or loss include financial assets held for trading and financial assets designated upon initial recognition at fair value through profit or loss. Financial assets are classified as held for trading if they are acquired for the purpose of selling in the near term. This category includes derivative financial instruments entered into by the Company that are not designated as hedging instruments in hedge relationships as defined by IAS 39. The Company has not designated any financial assets upon initial recognition as at fair value through profit or loss.

Derivatives, including separated embedded derivatives are also classified as held for trading unless they are designated as effective hedging instruments.

Financial assets at fair value through profit and loss are carried in the balance sheet at fair value with changes in fair value recognised in finance revenue or finance expense in the statement of comprehensive income.

##### **Loans and receivables**

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognised at fair value and subsequently measured at amortised cost using the EIR method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included in finance revenue in the income statement. Losses arising from impairment are recognised in the statement of comprehensive income in other operating expenses.



## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **Derecognition**

When the Company has transferred its rights to receive cash flows from an asset or has entered into a pass-through arrangement, it evaluates if and to what extent it has retained the risks and rewards of ownership. When it has neither transferred nor retained substantially all of the risks and rewards of the asset, and retained control of the asset, the Company continues to recognise the transferred asset to the extent of the Company's continuing involvement. In that case, the Company also recognises an associated liability. The transferred asset and the associated liability are measured on a basis that reflects the rights and obligations that the Company has retained.

#### **Financial assets**

##### **Debtors**

Debtors including amounts owed by group undertakings and other debtors, with no stated interest rate and receivable within one year are recorded at transaction price less provisions made for doubtful debts.

Provisions are made specifically where there is evidence of a risk of non-payment, taking into account ageing, previous losses experienced and general economic conditions.

##### **Loans to originator**

Where a transfer of a financial asset does not qualify for derecognition, the transferee does not recognise the transferred asset for financial reporting purposes, as its asset. The transferee derecognises the cash or other consideration paid and recognises a receivable from the transferor. In relation to the mortgage portfolio transferred to the Company, derecognition is considered to be inappropriate for the portfolio seller's or originator's (Southern Pacific Mortgage Limited) own financial statements as the originator has retained significant risks, in the form of credit enhancement paid in, and rewards, in the form of deferred purchase consideration to be paid out, of that financial asset. The Company's financial statements are therefore prepared on the basis that its acquisitions of beneficial interests in mortgage portfolios are recognised as a collateralised non-recourse loans to the originator.

The loans to originator are classified within debtors. The initial measurement is at fair value plus transaction costs that are directly attributable to the acquisition of the mortgage assets, with subsequent measurement being amortised cost using the EIR method. The effective interest on the loans to originator is calculated with reference to the interest earned on the mortgage assets underlying the loans to originator.

The loans to originator are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are carried at amortised cost using the EIR method, less impairment. Amortised cost is calculated by taking into account any discount or premium on acquisition and fees or costs that are an integral part of the EIR. The EIR amortisation is included in interest receivable and similar income in the statement of comprehensive income.

##### **Impairment of loans to originator**

The Company assesses at each statement of financial position date whether there is evidence that a mortgage asset underlying the loans to originator or a portfolio of financial assets is impaired. Impairment losses are recognised if, and only if, there is objective evidence of impairment as a result of one or more loss events that occurred after the initial recognition of the asset ("a loss event"), and that loss event or events has had an impact on the estimated future cash flows of the portfolio of financial assets or mortgage assets underlying the loans to originator that can be reliably estimated.

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

The Company assesses whether objective evidence of impairment exists for mortgage assets underlying the loans to originator on an individual loan basis. Those evaluations are based on the individual loan risk characteristics, taking into account: asset type; borrower; loan scores; geographical location; collateral type; past-due status; and other relevant factors. These characteristics are relevant to the estimation of future cash flows by being indicative of the counterparty's ability to pay all amounts due according to the contractual terms of the loan.

The amount of impairment loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The amount of the loss is recognised in the statement of comprehensive income.

Any impairment in the mortgage assets underlying the loans to originator will be reflected in the Company's accounts by adjusting the carrying amount of the loans to originator in the statement of financial position.

#### **Financial liabilities**

##### **Trade and other creditors**

Creditors including amounts owed to group undertakings, other creditors and accruals, with no stated interest rate and due within one year, are recorded at transaction price.

##### **Mortgage backed loan notes**

The mortgage backed loan notes were initially recognised at fair value, which was their par value at the date of issue less directly attributable transaction costs. The mortgage backed loan notes are subsequently remeasured at amortised cost taking into account repayments at interest payment dates where applicable.

Interest payable is recognised using the EIR method with the directly attributable transaction costs being amortised over the expected average life of the facility in line with IAS 39. Any unamortised issue costs are disclosed in note 16.

Interest payable on the notes during the year and any associated EIR adjustments are included in interest payable and similar expenses.

The repayment of the loan notes is dependent on principal and interest collections on the mortgage loans.

##### **Deferred consideration**

Deferred consideration is initially recognised at the fair value of the consideration paid.

Under the terms of the securitisation the Company earns a maximum annual profit for the year ended 30 November 2018 in an amount equal to 0.01% of the aggregate balance of the loans in the mortgage pool. Profits in excess of this amount accrue to the current holder of the rights to the residual cash flows of the securitisation as deferred consideration, unless the Company has cumulative adjusted losses from prior years. Accordingly, the amounts owing to the current holder of the rights to the residual cash flows of the securitisation are recognised as creditors in the Statement of Financial Position.

At each subsequent Statement of Financial Position date an accrual is made for deferred consideration within the financial statements as amounts are expected to become payable as a result of the performance of the mortgage assets underlying the loans to originator.

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **Offsetting of financial assets and liabilities**

In accordance with IAS 32 Financial Instruments: Presentation, the presentation of financial assets and financial liabilities are offset and the net amount is reported in the statement of financial position if there is a currently enforceable legal right to offset the recognised amounts and there is an intention to settle on a net basis, to realise the assets and settle the liabilities simultaneously.

#### **Fair value of financial assets and liabilities**

Fair value is 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 reporting date in the principal or, in its absence, the most advantageous market to which the Company has access at that date.

When available, the Company measures the fair value of an instrument using the quoted price in an active market for that instrument.

A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an on-going basis.

If there is no quoted price in an active market, then the Company uses valuation techniques that maximise the use of relevant observable inputs and minimise the use of unobservable inputs. The chosen valuation technique incorporates all of the factors that market participants would take into account in pricing a transaction.

Where applicable, the following methods are used to estimate the fair values of the financial instruments:

- i. cash, trade receivables and payables - the carrying value is a good approximation of the fair value;
- ii. fixed and variable rate borrowings - valued as detailed in note 18;
- iii. derivatives - net present value of the future cash-flows, calculated using market data at the statement of financial position date (principally exchange rates and yield curves); and
- iv. loans to originator - valued as detailed in note 18.

The Company, where appropriate, classifies disclosed fair values according to a hierarchy that reflects the significance of observable market inputs. A transfer is made between the hierarchy when the inputs have changed or there has been a change in the valuation method.

These fair value measurements are categorised into different levels in the fair value hierarchy based on the inputs to the valuation technique used.

The different levels are identified as follows:

Level 1 - quoted (unadjusted) prices in active markets for identical assets or liabilities.

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).

Level 3 - inputs for the asset or liability that are not based on observable market data (unobservable inputs).

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **Derivative financial instruments**

Where applicable the Company may use derivative financial instruments to hedge its exposure to interest rate risk and foreign exchange risk arising from financing and investment activities. The Company does not hold or issue derivative financial instruments for trading purposes. None of the economic hedge relationships held by the Company qualify for hedge accounting.

All derivative financial instruments are held at fair value through profit or loss. Subsequent to initial recognition, derivatives are remeasured to fair value. Where the value of the derivative is positive, it is carried as a derivative asset and, where negative, as a derivative liability. The gain or loss on remeasurement to fair value is recognised immediately in the statement of comprehensive income.

The fair value of the derivative financial instruments is the estimated amount that the Company would receive or pay to terminate the derivative contract at the statement of financial position date. Where derivative contracts contain collateral agreements which reduce counterparty risk the collateral is held in cash and recorded within creditors: due in less than one year (see note 15).

The counterparty risk from derivative transactions is taken into account when reporting the fair value of derivative positions. The adjustment to the fair value is known as the credit value adjustment (CVA). The Company's own risk of default is also incorporated into the fair value of derivative positions. This adjustment is known as the debit value adjustment (DVA). Neither adjustment has a material impact on the fair value of derivative positions.

#### **Currency swaps**

Where the Company holds non-Sterling denominated loan notes, the Company may enter into currency swaps in order to manage the Company's currency rate exposure. Where applicable, the derivative contracts are designed to match the expected profile of the run-off of the non-Sterling denominated loan notes.

Details of any derivatives held by the Company are disclosed in note 18.

#### **2.7. Premium paid on mortgage assets underlying the loans to originator**

A premium is recognised where mortgage assets underlying the loans to originator are acquired at amounts in excess of their carrying values. Where this occurs the premium is capitalised by the Company and amortised over the expected repayment period of the mortgage assets underlying the loans to originator. The amortised balance is added to the loans to originator balance with the costs amortised in the period included in interest receivable and similar income. Details of any unamortised premiums paid on mortgage assets underlying the loans to originator are disclosed in note 13.

#### **2.8. Discount on purchase of mortgage assets underlying the loans to originator**

Where cash has been received from the originator on acquisition of the mortgage assets underlying the loans to originator to cover start-up costs, it is amortised over the expected life of those mortgage assets. The amortised balance is deducted from the loans to originator with the income for the year included in interest receivable and similar income. Details of any unamortised discounts on acquisition of mortgage assets underlying the loans to originator are disclosed in note 13.

#### **2.9. Segmental analysis**

The Company's income and trade are wholly within the United Kingdom and within a single market sector and therefore no segmental analysis has been presented.

#### **2.10. Cash and cash equivalents**

Cash and cash equivalents in the statement of financial position comprise cash at banks and in hand and short-term deposits with a maturity of three months or less.

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **2.11. Share capital and capital contributions**

Ordinary shares are classified as equity. Incremental costs directly attributable to the issue of new shares or options are shown in equity as a deduction net of tax from the proceeds.

#### **3 Significant accounting estimates and judgements**

The preparation of financial statements in accordance with FRS 101 requires management to make judgements, estimates and assumptions that affect the reported amounts of revenues, expenses, assets and liabilities, and the accompanying disclosures of contingent liabilities. Uncertainty about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of assets or liabilities affected in future periods.

##### **3.1. Significant accounting judgements**

###### **Derecognition of mortgage assets**

The Company has made a significant accounting judgement in the assessment of the loans to originator. The Company performed an assessment of the risks and rewards associated with the financial assets acquired, and concluded that the financial assets qualify for derecognition for the originator. In making this assessment the Company considered the retained risks of the seller, in the form of credit enhancement paid in, and rewards, in the form of deferred purchase consideration to be paid out, of that financial asset. This follows the accounting treatment adopted in the sellers' financial statements.

##### **3.2. Significant accounting estimates and assumptions**

The Company has identified the following significant accounting policies that involve significant accounting estimates and assumptions:

###### **Impairment of loans to originator**

Impairment losses on loans to originator are calculated based on statistical models. The key assumptions relate to estimates of future cash flows from customers' accounts, their timing and, for secured accounts, the expected proceeds from the realisation of the property. These key assumptions are based on observed data from historical patterns and are updated regularly based on new data as it becomes available.

In addition the directors consider how appropriate past trends and patterns might be in the current economic situation and make any adjustments they believe are necessary to reflect current conditions.

The accuracy of the impairment calculations would therefore be affected by unexpected changes to the economic situation, variances between the models used and the actual results, or assumptions which differ from the actual outcomes. In particular, if the impact of economic factors such as employment levels on customers is worse than is implicit in the model then the number of accounts requiring provision might be greater than suggested by the model, while falls in house prices, over and above any assumed by the model might increase the provision required in respect of accounts currently provided.

A decrease in the House Price Index of 10% spread over the next 2 years increases the mortgage asset impairment provision by £491,000.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### Effective Interest Rate ("EIR")

The EIR is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the net carrying amount of the financial asset or liability. When calculating the effective interest rate, the Company estimates future cash flows considering all contractual terms of the financial instrument, but not future credit losses. The cash flows used to calculate the EIR in this analysis include directly attributable transaction costs, premiums, discounts and the impact of changes from introductory to reversionary interest rates.

The book value of the mortgage assets underlying the loans to originator is measured at amortised cost using the EIR method, with a provision made for impairment. The current model used to estimate future cash flows in the EIR is sensitive to certain key assumptions, the most important of which is the constant prepayment rate ("CPR").

An increase of 1% in the CPR assumed would result in a loss of £450,000.

#### Fair value measurement

Where applicable, the Company measures financial instruments, such as derivatives, at fair value at each statement of financial position date. For the valuation of derivative financial instruments, a discounted cash flow model is used based on a current interest rate yield curve. The yield curve is the primary determinant of the valuation, and is constructed by benchmarking to generic instruments in the market that are sensitive to overnight index swap ("OIS") movements. Details of the fair value measurement of any derivative financial instruments held by the Company are included in note 18.

#### 4 Interest receivable and similar income

	2018 £'000	2017 £'000
Interest receivable on loans to originator	6,027	2,676
Amortisation of premium/discount on mortgage assets underlying the loans to originator	196	263
Other interest	17	(14)
	<u>6,240</u>	<u>2,925</u>

The estimated weighted average life of the mortgage assets underlying the loans to originator is 5.3 years (2017: 5.4 years). During the year the impact of the change in the estimated weighted average life on the effective interest rate calculation resulted in a gain of £1,622,000 (2017: loss of £1,884,000).

Interest has accrued for the year in relation to impaired financial assets at 4.78% (2017: 4.16%) of the principal balance.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### 5 Interest payable and similar expenses

	2018 £'000	2017 £'000
Interest expense on loan notes	724	472
Amortisation of capitalised issue costs	29	34
Amortisation of premium on mortgage assets underlying the loans to originator	-	34
	<u>753</u>	<u>540</u>

#### 6 Other operating income

	2018 £'000	2017 £'000
Redemption fees	3	5
Sundry fee income	8	-
	<u>11</u>	<u>5</u>

#### 7 Loss before taxation

	2018 £'000	2017 £'000
Loss before taxation is stated after charging/(crediting):		
Auditor's remuneration for statutory audit	11	22
Impairment credit on mortgage assets underlying the loans to originator	(131)	(376)
Amounts written off on mortgage assets underlying the loans to originator	26	202
Deferred consideration	4,654	5,087
Mortgage administration fees	<u>81</u>	<u>189</u>

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### 8 Taxation

	2018 £'000	2017 £'000
<b>Analysis of tax expense for the year</b>		
<b>Current tax</b>		
UK corporation tax expense on loss for the year	2	2
Adjustments in respect of prior periods	4	-
<b>Total current tax</b>	<u>6</u>	<u>2</u>
<b>Deferred tax</b>		
Origination and reversal of timing differences	(143)	(806)
Effect of changes in tax rates	-	5
<b>Total deferred tax</b>	<u>(143)</u>	<u>(801)</u>
<b>Tax credit on loss</b>	<u>(137)</u>	<u>(799)</u>

#### Factors affecting taxation

The tax assessed for the year is higher than (2017: higher than) the standard rate of corporation tax in the United Kingdom of 19.00% (2017: 19.33%).

	2018 £'000	2017 £'000
Loss before tax	<u>(738)</u>	<u>(4,161)</u>
Loss multiplied by the standard rate of corporation tax in the UK of 19.00% (2017: 19.33%)	(141)	(804)
<b>Effects of:</b>		
Effect of changes in tax rates	-	5
Adjustment in respect of prior periods	4	-
<b>Tax credit for the year</b>	<u>(137)</u>	<u>(799)</u>

The Finance Act 2016 contains provisions reducing the rate of United Kingdom corporation tax from 19% to 17% from 1 April 2020. This Act was substantively enacted on 15 September 2016.

#### 9 Directors and employees

The Company does not have any employees other than the directors (2017: none). The directors' did not receive any remuneration in the year (2017: nil).



## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### 10 Loans to originator - net of impairment

	Loans to originator £'000	Impairment £'000	Loans to originator, net of impairment £'000
At 1 December 2016	123,174	(1,075)	122,099
Movement in the year	(12,812)	376	(12,436)
At 30 November 2017	110,362	(699)	109,663
Movement in the year	(9,020)	131	(8,889)
<b>At 30 November 2018</b>	<b>101,342</b>	<b>(568)</b>	<b>100,774</b>

The loans to originator are denominated in Sterling and bear interest at a variable rate. They are secured on the beneficial interest in the portfolio of residential mortgage loans.

The current mortgage loans in the pool have contractual loan periods of between 1 to 281 (2017: 1 to 293) months remaining with current interest rates ranging from 0.00% to 14.81% (2017: 0.00% to 14.28%) per annum.

The book value of the mortgage assets underlying the loans to originator are measured at amortised cost using the EIR method, with a provision made for impairment. The impairment provision is a specific provision of £568,000 (2017: £699,000). The impairment model used to estimate future cash flows in the impairment calculation is sensitive to certain key assumptions being the expected probability of default, the expected time to move through the arrears/repossession cycle and expected recovery rates on losses incurred.

A decrease in the House Price Index of 10% spread over the next 2 years increases the mortgage asset impairment provision by £491,000.

#### 11 Debtors: amounts falling due after more than one year

	2018 £'000	2017 £'000
Loans to originator net of impairment (note 10)	88,420	96,974
	<u>88,420</u>	<u>96,974</u>

#### 12 Debtors: amounts falling due within one year

	2018 £'000	2017 £'000
Loans to originator net of impairment (note 10)	12,354	12,689
Amounts due from group companies	-	18
Prepayments and accrued income	4	1
Other debtors	28	12
	<u>12,386</u>	<u>12,720</u>

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

Amounts due from group undertakings are interest free and repayable on demand.

Loans to originator net of impairment represent the portion of the mortgage book expected to repay over the next 12 months based on behavioural analysis performed.

#### 13 Premium/discount on mortgage assets underlying the loans to originator

	2018 £'000	2017 £'000
<b>Premium on acquisition of mortgages</b>		
At 1 December	184	218
Amortisation in the year	(29)	(34)
At 30 November	<u>155</u>	<u>184</u>

The premium paid on mortgage assets is amortised in line with the amortisation profile of the mortgage assets. The amortisation charges are recognised within interest receivable in the statement of comprehensive income.

	2018 £'000	2017 £'000
<b>Discount on acquisition of mortgages</b>		
At 1 December	(1,422)	(1,685)
Amortisation in the year	225	263
At 30 November	<u>(1,197)</u>	<u>(1,422)</u>

The discount on mortgage assets underlying the loans to originator is amortised in line with the amortisation profile of the mortgage assets. The amortisation charges are recognised within interest receivable in the statement of comprehensive income.

#### 14 Cash and cash equivalents

	2018 £'000	2017 £'000
Cash at bank and in hand	<u>11,488</u>	<u>13,568</u>
	<u>11,488</u>	<u>13,568</u>

Cash at bank earns interest at the rates specified in note 18.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### 15 Creditors: amounts falling due within one year

	2018	2017
	£'000	£'000
Accruals and deferred income	785	756
Other creditors	34	83
Amounts owed to group undertakings	65	66
Deferred consideration	13,113	11,167
Collateral accounts	4,630	7,150
	<u>18,627</u>	<u>19,222</u>

Amounts due to group undertakings are interest free and payable on demand.

A monthly accrual is made in the statement of comprehensive income for deferred consideration that will ultimately become payable. Under the terms of the waterfall of payments, any deferred consideration would only be paid when there are sufficient revenue funds available and all other liabilities in the waterfall have been satisfied. Deferred consideration is paid on a quarterly basis based on available revenue funds.

As at 30 November 2018, the Company held £4,630,000 (2017: £7,150,000) of cash, including interest, as collateral as a result of the downgrading of certain counterparties' credit ratings. The right to the cash remains with the swap counterparty and a collateral creditor has this been recognised. Collateral accounts accrue interest at published overnight currency interest rates and are repayable in the event the swap counterparty's credit rating exceeds pre-determined thresholds.

#### 16 Creditors: amounts falling due after more than one year

	2018	2017
	£'000	£'000
EUR Denominated mortgage backed loan notes due 2044 -Class A3a	14,981	21,908
GBP Denominated mortgage backed loan notes due 2044 -Class A3c	10,582	15,565
EUR Denominated mortgage backed loan notes due 2044 -Class B1a	43,289	43,037
EUR Denominated mortgage backed loan notes due 2044 -Class C1a	17,742	17,638
GBP Denominated mortgage backed loan notes due 2044 -Class C1c	9,850	9,850
EUR Denominated mortgage backed loan notes due 2044 -Class D1a	5,367	5,336
GBP Denominated mortgage backed loan notes due 2044 -Class D1c	11,000	11,000
GBP Denominated mortgage backed loan notes due 2044 -Class E1c	4,080	4,080
Total loan notes	<u>116,891</u>	<u>128,414</u>
Less unamortised issue costs	<u>(155)</u>	<u>(184)</u>
	<u>116,736</u>	<u>128,230</u>

The mortgage backed loan notes due in 2044 are secured over the portfolio of mortgage assets secured by first and second charges over residential properties in the United Kingdom.

The mortgage assets underlying the loans to originator are administered by Acenden Limited on behalf of the Company.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

The mortgage backed loan notes are repaid as the underlying portfolio redeems. The terms and conditions of the mortgage backed loan notes provide that the loan note holders will receive interest and principal only to the extent that sufficient funds are generated from the mortgage assets underlying the loans to originator.

None (2017: none) of the mortgage backed loan notes are owed to a related party.

Whilst the mortgage backed loan notes are subject to mandatory redemption in part at each Interest Payment Date in an amount equal to the principal received or recovered in respect of the mortgage assets underlying the loans to originator, the mortgage backed loan notes are classified and presented as amounts falling due after one year in accordance with the contractual maturity dates due to the uncertainty in the expected principal repayments or recoveries of the mortgages. If not otherwise redeemed or purchased and cancelled, the mortgage backed loan notes will be redeemed at their principal amount outstanding on the Interest Payment Date falling in 2044.

The priority and amount of claims on the portfolio proceeds are determined in accordance with a strict priority of payments. The mortgage backed loan notes are repayable out of capital receipts from the mortgage assets underlying the loans to originator, with the Class A Notes ranking in priority to the Class B Notes, which rank in priority to the Class C Notes, which rank in priority to the Class D Notes, which rank in priority to the Class E Notes.

Interest on the loan notes is payable quarterly in arrears at the following annual rates for three month deposits:

Class A3a	EURIBOR + 0.17%
Class A3c	Sterling LIBOR + 0.17%
Class B1a	EURIBOR + 0.25%
Class C1a	EURIBOR + 0.45%
Class C1c	Sterling LIBOR + 0.45%
Class D1a	EURIBOR + 0.90%
Class D1c	Sterling LIBOR + 0.90%
Class E1c	Sterling LIBOR + 3.25%

A call option exists over the notes which may be exercised at the sole discretion of the issuer (with the approval of the trustee) once the outstanding mortgage backed loan notes reach 10% of the original issued amount. The threshold has not been satisfied.

#### 17 Deferred tax

	2018 £'000	2017 £'000
Opening deferred tax balance	296	(505)
Origination and reversal of temporary differences	143	806
Rate change in respect of temporary differences	-	(5)
Closing deferred tax balance	439	296

Deferred taxation has been recognised at 19.00% (2017: 19.00%) being the UK corporation tax rate expected to apply in the period in which the timing differences are expected to reverse based on the tax rates that have been enacted at the statement of the financial position date.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

The deferred tax balance is made up as follows:

	2018 £'000	2017 £'000
Short term timing differences	439	296
	<u>439</u>	<u>296</u>

#### 18 Financial instruments and risk management

##### Nature and extent of risks arising from financial statements

The main risks arising from the Company's financial instruments are credit risk, liquidity risk, foreign currency risk, interest rate risk and operational risk as explained in the strategic report. Financial instruments used by the Company for risk management purposes include derivative instruments. Such instruments are used only for commercial hedging purposes, not for trading or speculative purposes. The principal derivative instruments used by the Company in managing its risks are foreign currency swaps. The maturity profile of the derivative instruments reflects the nature of exposures arising from underlying business activities. All of the Company's derivatives activities are contracted with financial institutions.

During the year, the Company recognised a loss of £1,211,000 (2017: loss of £981,000) due to the movements in the fair value of derivatives and exchange rate movements on the loan notes.

##### a) Credit risk

The underlying mortgages are classified as loans to originators, this means that in the first instance the recovery of the debt is against the originating company. The mortgages are fully secured against the loan and therefore ring fenced from other creditors in the originating company and the originating company is bound under the contractual terms to pay across the cash flows from the underlying loans, therefore credit risk is assessed as being against the underlying mortgages.

Credit risk is the risk that borrowers of the mortgage assets underlying the loans to originator will not be able to meet their obligations as they fall due. All mortgage assets underlying the loans to originator are required to adhere to specific lending criteria. The payments in respect of the financial instruments are dependent upon the performance of the mortgage assets underlying the loans to originator. The ongoing credit risk of the mortgage portfolio (and particularly in respect of accounts in arrears) is closely monitored by the directors.

The level of arrears in the mortgage portfolio has largely stabilised, which the directors consider is consistent with the improvement in the market conditions experienced in the past few years in the United Kingdom mortgage market. Arrears management and recovery processes are performed with the aim of maximising customer rehabilitation. Whilst there has been strong arrears performance, the directors acknowledge that market conditions, resulting in a benign interest rate environment, has partly contributed to the strong portfolio performance. With this in mind, the directors continue to closely monitor the economic landscape to ensure the Company is best placed to respond to any pressures that may impact portfolio performance and proactively consider strategies to mitigate any adverse portfolio impact should these pressures occur.

Credit quality of the mortgage assets underlying the loans to originator is assessed by an assessment of each customer and the prevailing macroeconomic environment. Probability of default of the customer and the loss given default is calculated and impairment provisions raised where necessary.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

Before taking account of any collateral, the maximum exposure to credit risk as at 30 November 2018 was:

	2018 £'000	2017 £'000
Loans to originator	101,342	110,362
Cash and cash equivalents	11,488	13,568
Derivative financial instruments	20,825	22,690
	<u>133,655</u>	<u>146,620</u>

#### Collateral accounts

At 30 November, the Company held £4,630,000 (2017: £7,150,000) of cash, including interest, as collateral as a result of the downgrading of certain swap counterparties' credit ratings. The right to the cash remains with the swap counterparty and a collateral creditor has been recognised. Collateral accounts accrue interest at published overnight currency interest rates and are repayable in the event the swap counterparty's credit rating exceeds pre-determined thresholds.

#### Loans to originator and asset credit quality

All mortgage assets underlying the loans to originator are categorised, as either 'neither past due nor impaired', 'past due but not impaired', or 'past due and impaired'. A loan is considered past due when the borrower has failed to make a payment when due under the terms of the loan contract.

As at 30 November 2018, the ageing analysis of mortgage assets underlying the loans to originator is as follows:

	2018 £'000	2017 £'000
Neither past due nor impaired	53,960	63,207
Past due but not impaired – less than 30 days	6,854	2,173
Past due but not impaired – between 30 and 60 days	4,745	1,132
Past due but not impaired – between 61 and 90 days	2,142	157
Past due but not impaired – between 91 and 120 days	2,143	138
Past due but not impaired – more than 120 days	2,498	647
Impaired	29,000	42,908
Total	<u>101,342</u>	<u>110,362</u>

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

The mortgage assets underlying the loans to originator have the following loan to value ("LTV") profile based on indexed valuations of the underlying properties, giving an indication of their credit quality:

	2018 £'000	2017 £'000
0-50%	52,710	54,088
50.01% - 70%	29,110	33,036
70.01% - 90%	18,336	21,245
90.01% - 100%	829	1,428
Over 100%	357	565
Total	101,342	110,362

The portfolio of mortgage assets is well diversified geographically with the highest exposure being in London at 12.84% (2017: South East at 16.00%).

#### b) Liquidity risk

The undiscounted estimated cash flows associated with financial liabilities were as follows:

As at 30 November 2018 Financial liabilities	Less than 1 year £'000	1-2 years £'000	2-3 years £'000	3-4 years £'000	4-5 years £'000	5+ years £'000	Total £'000
Loan notes	16,716	14,717	17,583	9,856	9,564	57,344	125,780
Currency swap collateral	4,630	-	-	-	-	-	4,630

As at 30 November 2017 Financial liabilities	Less than 1 year £'000	1-2 years £'000	2-3 years £'000	3-4 years £'000	4-5 years £'000	5+ years £'000	Total £'000
Loan notes	16,979	16,236	14,008	18,238	9,672	62,122	137,255
Currency swap collateral	7,150	-	-	-	-	-	7,150

There is no contractual obligation to pay down the loan notes other than as set out in note 16.

The estimated future cash flows are sensitive to certain key assumptions being the expected probability of default, the expected time to move through the arrears/repossession cycle and expected recovery rates on losses incurred. Future cash flows have been estimated using a combination of macro environmental factors, including market observable data, and individual borrower data. However, it is not expected that the loans will repay at a constant rate until maturity, that all of the loans will prepay at the same rate or that there will be no defaults or delinquencies on the loans, therefore the amounts disclosed above are only estimates of the possible future cash outflows on the loan notes.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

In addition, the Company holds a minimum cash balance to manage short term liquidity requirements which can be used in certain circumstances. The undiscounted cash flows have been estimated by previously applying a constant (per annum) prepayment rate to the principal balance of the mortgage loans and using the weighted average interest rate prevailing at the statement of financial position date.

The loan notes in the above table will not agree to the liability in statement of financial position as the table incorporates both principal and interest payments on an undiscounted basis (see note 16 for maturity dates). For the current and the prior year, all mortgage backed loan notes are due in more than 5 years, and all other non-derivative creditors are repayable on demand.

The Company's policy is to manage liquidity risk by matching cash payments due on the mortgage backed loan notes to cash receipts from mortgage assets.

#### c) Foreign currency risk

With the exception of certain mortgage backed loan notes and cross currency swaps, as shown below, all financial instruments are denominated in Sterling. The outstanding mortgage backed loan notes include the following foreign currency denominated balances:

	2018 Notional amount €'000	2017 Notional amount €'000
EUR Denominated mortgage backed loan notes due 2044 -Class A3a	16,889	24,841
EUR Denominated mortgage backed loan notes due 2044 -Class B1a	48,800	48,800
EUR Denominated mortgage backed loan notes due 2044 -Class C1a	20,000	20,000
EUR Denominated mortgage backed loan notes due 2044 -Class D1a	6,050	6,050
	<u>91,739</u>	<u>99,691</u>

A series of currency swaps have been entered into, in order to manage the Company's currency rate exposure in relation to non-Sterling denominated backed loan notes.

The following is the profile of the Company's currency swaps:

	2018 Notional amount €'000	2017 Notional amount €'000
Euro denominated currency swaps	<u>91,739</u>	<u>99,691</u>

The Company is not materially exposed to foreign exchange risk as the currency swap notional amount matches the notional amount of the euro denominated mortgage backed loan notes.

The fair value of the currency swaps are disclosed in note 18 (this note) Fair value of derivatives. The maturity profile of the foreign currency swaps is consistent with the mortgage backed loan notes.



## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### d) Interest rate risk

##### Interest rate risk profile of financial assets

	Total £'000	Total variable rate £'000	Total fixed rate £'000	Weighted average interest rate* %	Weighted average time for which rate is fixed Years
<b>2018</b>					
Loans to originator	101,342	101,342	-	4.49	-
Cash at bank and in hand	11,488	-	11,488	0.12	0.25
Currency swaps	20,825	20,825	-	-	-
<b>2017</b>					
Loans to originator	110,362	110,362	-	3.97	-
Cash at bank and in hand	13,568	-	13,568	0.00	0.25
Currency swaps	22,690	22,690	-	-	-

\* This is the weighted average spread above LIBOR.

\*\* The derivatives are shown at fair value. The corresponding notional amounts are disclosed in note 18 (this note): Fair value of derivatives.

##### Interest rate sensitivity analysis on financial assets

	Increase in basis points	Effect on equity £'000	Effect on result before tax £'000
<b>2018</b>			
Loans to originator	25	253	253
Cash at bank and in hand	25	29	29
<b>2017</b>			
Loans to originator	25	276	276
Cash at bank and in hand	25	34	34

The assumed movement in basis points for interest rate sensitivity analysis is based on the currently observable market conditions. In assessing the effect on financial assets of interest rate sensitivity, management have used a benchmark of 25 bps.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### Interest rate risk profile of financial liabilities

	Total	Total variable rate	Weighted average Interest rate
	£'000	£'000	%
<b>2018</b>			
Mortgage backed loan notes	116,891	116,891	0.48
Currency swap collateral	4,630	4,630	-
<b>2017</b>			
Mortgage backed loan notes	128,414	128,414	0.45
Currency swap collateral	7,150	7,150	-

Interest payable on the mortgage backed loan notes and receivable on mortgage assets underlying the loans to originator are both based on LIBOR. Whilst certain mortgage backed loan notes are denominated in foreign currency and incur interest based on EURIBOR (EUR notes) the Company has entered into currency swap agreements which allows the Company to settle its note liability obligations with reference to LIBOR. The Company thus has limited exposure to interest rate risk.

The interest rate risk profile of the mortgage backed loan notes in issue can be found in note 16. The Company's approach to managing interest rate risk is included in the principal risks and uncertainties section of the strategic report.

#### Interest rate sensitivity analysis on financial liabilities

	Increase in basis points	Effect on equity £'000	Effect on result before tax £'000
<b>2018</b>			
GBP loan notes	25	(89)	(89)
EUR loan notes	25	(203)	(203)
<b>2017</b>			
GBP loan notes	25	(101)	(101)
EUR loan notes	25	(220)	(220)

In assessing the effect on financial liabilities of interest rate sensitivity, management have used a benchmark of 25 bps.

The Company also has certain financial instruments included within debtors (note 12) and creditors (note 15) which are not subject to interest rate risk as they bear no interest.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### Interest income and expense on financial instruments that are not at fair value through profit and loss

	2018 £'000	2017 £'000
Interest receivable on loans to originator	6,027	2,676
Interest expense on loan notes	(724)	(472)
	<u>5,303</u>	<u>2,204</u>

#### e) Operational risk

Operational risk is defined as any instance where there is potential or actual impact to the Company resulting from inadequate or failed internal processes, people, systems, or from external events. The impacts can be financial as well as non-financial such as customer detriment, reputational or regulatory consequences.

The Company operates under a controls and governance framework provided by the servicer of the mortgage assets underlying the loans to originator. This includes regulatory and compliance functions and internal audit. The business is covered by the servicer's business continuity management capability.

#### f) Fair values of financial assets and liabilities

	2018 Book value £'000	2018 Fair value £'000	2017 Book value £'000	2017 Fair value £'000
<b>Financial assets</b>				
Loans to originator	100,774	104,466	109,663	118,430
Cash at bank and in hand				
Reserve and contingency funds	2,550	1,575	2,550	1,461
Other cash balances	8,938	8,938	11,018	11,018
	<u>11,488</u>	<u>10,513</u>	<u>13,568</u>	<u>12,479</u>
Derivative financial instruments	20,825	20,825	22,690	22,690
	<u>133,087</u>	<u>135,804</u>	<u>145,921</u>	<u>153,599</u>
<b>Financial liabilities</b>				
Mortgage backed loan notes	116,891	106,150	128,414	118,411
Deferred consideration	13,113	13,113	11,167	11,167
Swap collateral creditor	4,630	4,630	7,150	7,150
	<u>134,634</u>	<u>123,893</u>	<u>146,731</u>	<u>136,728</u>

All financial assets and liabilities are held at amortised cost, except for derivative financial instruments that are held at fair value. There were no transfers between categories in both periods. Management have assessed all other assets and liabilities and consider book value to be equal to fair value.

Management does not expect any losses from non-performance by the counterparties holding cash and cash equivalents. There are no material differences between their book values and fair values.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

The directors have considered the fair values of the Company's main financial instruments which are loans to originator, mortgage backed loan notes, derivative financial instruments and cash.

The fair value of the mortgage backed loan notes has been based upon their quoted prices; where available, or prices interpolated using latest available market data. The fair value of the loans to originator has been based upon the fair value of the mortgages underlying the loan notes, and expected residual cash flows. It is the opinion of the directors that this methodology is appropriate as the market is more liquid than in prior years.

As part of the process of assessing fair value, management have refined the assumptions used. This has been achieved using a combination of macro environmental factors including market observable data and individual borrower data resulting in a more accurate reflection of the estimated cash flows used for computing fair value.

Mortgage backed loan notes and loans to originator are classified as level 2 and level 3 respectively.

#### Fair value of derivatives

	2018 Notional amount £'000	2018 Assets £'000	2018 Liabilities £'000	2017 Notional amount £'000	2017 Assets £'000	2017 Liabilities £'000
Currency swaps	81,379	<u>20,825</u>	<u>-</u>	87,919	<u>22,690</u>	<u>-</u>
		<u>20,825</u>	<u>-</u>		<u>22,690</u>	<u>-</u>

The Company recognised a loss on the fair value of derivatives of £703,000 during the year (2017: gain of £2,808,000).

For the valuation of derivative financial instruments, a discounted cash flow model is used based on a current interest rate yield curve. The yield curve is the primary determinant of the valuation, and is constructed by benchmarking to generic instruments in the market that are sensitive to Overnight Index Swap ("OIS") movements. Consequently, the Company deems all its derivative financial instruments to be level 2.

The Company does not have other financial instruments held at fair value and there have been no transfers between levels within the fair value hierarchy.

The rates of interest receivable and payable on variable rate financial instruments, with the exception of the non-Sterling denominated mortgage backed loan notes, are set with reference to the London Interbank Offer Rate ("LIBOR"). The rates of interest payable on the mortgage backed loan notes are set as detailed in note 16.

## Eurosail 2006-3NC plc

### Notes to the financial statements for the year ended 30 November 2018

#### 19 Share capital

	2018 £	2017 £
<b>Authorised, allotted, called up and fully paid:</b>		
2 ordinary 100% called and fully paid shares of £1 each	<u>2</u>	<u>2</u>
<b>Authorised, allotted, called up and partly paid:</b>		
49,998 ordinary 25% called and paid shares of £1 each	<u>12,500</u>	<u>12,500</u>

#### 20 Related party transactions

The transactions and outstanding balances arose in the ordinary course of business and on substantially the same terms, including interest rates and security, as for comparable transactions with persons of a similar standing. None of the outstanding balances have been impaired.

	Amount expensed 2018 £'000	Amount outstanding 2018 £'000	Amount expensed 2017 £'000	Amount outstanding 2017 £'000
<b>Southern Pacific Mortgage Limited</b>				
Mortgage related amounts payable	-	(66)	-	(66)
Deferred consideration	(4,654)	(13,113)	(5,087)	(11,167)
Loans to originator	-	100,774	-	109,663
Interest receivable on loans to originator	6,027	-	2,676	-
<b>Wilmington Trust SP Services (London) Limited</b>				
Corporate Services fees	(12)	-	(20)	-
	<u>1,361</u>	<u>87,595</u>	<u>(2,431)</u>	<u>98,430</u>

## **Eurosail 2006-3NC plc**

### **Notes to the financial statements for the year ended 30 November 2018**

#### **21 Parent undertaking and control**

The Company's immediate parent undertaking is Eurosail 2006-3NC Parent Limited which is registered and operates in England, United Kingdom and has its registered office located at Third Floor, 1 King's Arms Yard, London, EC2R 7AF. The entire issued share capital of Eurosail 2006-3NC Parent Limited is held by a trustee under a declaration of trust for charitable purposes.

An affiliate company, Southern Pacific Mortgage Limited, retains an interest in the cash flows and profits of the Company. The Company's operations are managed by Wilmington Trust SP Services (London) Limited, an affiliate company.

The largest and smallest group in which the results of the Company are consolidated is Southern Pacific Mortgage Limited, a Company incorporated in England, United Kingdom. The consolidated financial statements of Southern Pacific Mortgage Limited are available to the public and may be obtained from Registrar of Companies, Companies House, Crown Way, Maindy, Cardiff CF14 3UZ.

The Company's ultimate controlling party is Lehman Brothers Holdings Inc., which is incorporated in the state of Delaware in the United States of America, and is the ultimate parent undertaking of Southern Pacific Mortgage Limited. On 15 September 2008, the ultimate controlling party Lehman Brothers Holdings Inc., filed for Chapter 11 bankruptcy protection.

#### **22 Capital management**

The Company is not subject to any externally proposed capital requirements except for the minimum requirement under the Companies Act 2006. The Company has not breached the minimum requirement.

The Company's capital consists of share capital contributed by investors. Due to the structural features of the securitisation process, where cash paid out to noteholders cannot exceed cash received, and where the holder of the deferred consideration certificate is entitled to any excess deferred consideration, the amount of share capital is not expected to fluctuate over time. Accordingly, the objective of capital management is to hold constant the amount of share capital, and this objective is achieved by the structural features of the securitisation transaction documented in the offering circular and other legal documentation.

#### **23 Contingent liabilities**

There are no (2017: nil) contingent liabilities or commitments at the year end or up to the date of signing the directors' report.

#### **24 Post balance sheet date events**

There are no significant events occurring after the statement of financial position date, up to the date of approval of the financial statements that would meet the criteria to be disclosed or adjusted in the financial statements as at 30 November 2018.