

Company Registration Number 5990966

DECO 11 – UK CONDUIT 3 PLC
ANNUAL REPORT AND FINANCIAL STATEMENTS
FOR THE YEAR ENDED 31 DECEMBER 2016

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DECO 11 – UK CONDUIT 3 PLC

ANNUAL REPORT AND FINANCIAL STATEMENTS FOR THE YEAR ENDED 31 DECEMBER 2016

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DECO 11 – UK CONDUIT 3 PLC

COMPANY INFORMATION

The board of directors

Mr Graham Cox
Mr Graham Hodgkin

Company secretary

Sunil Masson

Registered office

Winchester House
Mailstop 428
1 Great Winchester Street
London
EC2N 2DB

Auditor

Deloitte LLP
Statutory Auditor
London
United Kingdom

DECO 11 – UK CONDUIT 3 PLC

STRATEGIC REPORT

FOR THE YEAR ENDED 31 DECEMBER 2016

The directors present their strategic report together with the audited financial statements of Deco 11 – UK Conduit 3 Plc (the “Company”) for the year ended 31 December 2016.

REVIEW OF THE BUSINESS

The Company was incorporated as a public company with limited liability on 7 November 2006 under the laws of England and Wales. The Company was established as a special purpose Company for the purposes of issuing floating rate loan notes (the “loan notes”) due January 2020. The loan notes comprise Class A-1A notes, Class A-1B notes, Class A-2 notes, Class B notes, Class C notes, Class D notes, Class E notes and Class F notes with Class A-1A notes bearing the highest ranking in priority. On 20 December 2006, the Company issued £444,387,935 loan notes in accordance with the Offering Circular dated 19 December 2006.

The Company used the proceeds from the issue of these loan notes to acquire the beneficial interest in a commercial mortgage portfolio from Deutsche Bank AG, London Branch, (the “mortgage loans”), to open accounts, to create security and receive interest in respect thereof, and to enter into certain related transactions as described in the Offering Circular.

The loan notes are listed on the Irish Stock Exchange.

The directors do not anticipate any other changes to the present level of activity. However as disclosed below there is a material uncertainty that may cast significant doubt about the Company’s ability to continue as a going concern.

RESULTS AND PERFORMANCE

The results of the Company for the year, as set out on page 12, show a loss on ordinary activities before tax of £26,890,921 (2015: profit of £35,469,035). The loss was primarily due to an impairment charge of £29,326,119 (2015: reversal of £28,210,831). The Company had a shareholder’s deficit of £140,345,967 (2015: £113,454,793) as at 31 December 2016. The deficit was primarily due to the cumulative impairment on the mortgage loans of £130,307,818 (2015: £95,891,874).

STRATEGY

The principal activity of the Company is the issue of loan notes. The Company has issued loan notes to fund the acquisition of beneficial interest in a mortgage loan portfolio. These financial assets and liabilities provide the majority of the assets and liabilities of the Company along with associated interest income and expense.

The strategies used by the Company in achieving its objectives regarding the use of their financial instruments were set when the Company issued the loan notes. The principal risks arising from the Company’s financial instruments (both assets and liabilities) are credit risk, interest rate risk, refinancing risk and liquidity risk.

The Company has also entered into swap agreements. This is to mitigate the interest rate risk associated with the mismatch between the fixed and floating rate interest generated by the mortgage loans and the floating rate on the loan notes.

KEY PERFORMANCE INDICATORS (‘KPIs’)

The key performance indicator of the business is considered to be the net interest margin. During the year, the Company achieved a net interest margin (net interest income divided by interest income) of -62.64% (2015: 14.80%). The decrease in the net interest margin is mainly attributed to the decrease in interest income due to default on interest payments by the loan holders and the adjustment to interest income due to effective interest rate (note 2).

DECO 11 – UK CONDUIT 3 PLC

STRATEGIC REPORT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES

The directors acknowledge that during the year under review, the United Kingdom economy grew more than previously forecasted propelled by a buoyant services sector and a rise in exports likely due to a weaker currency. 2017 is likely to see a slowdown in growth with uncertainty regarding the United Kingdom's future relationship with the European Union deterring investment and a moderation in household income growth dampening private consumption. However, the Bank of England's accommodative monetary policy stance will cushion the decline. These factors are likely to affect the performance of the Company.

The Company's financial instruments, other than derivatives, comprise mortgage loans, cash and cash equivalents, loan notes and various receivables and payables that arise directly from its operations. The main purpose of the interest bearing borrowings is to finance a mortgage portfolio acquired from Deutsche Bank AG, London Branch.

The Company also enters into derivative transactions. The purpose of such transactions is to manage the interest rate risk arising from the Company's operations and its sources of finance.

The Board reviews and agrees policies for managing risks arising on the Company's financial instruments and they are summarised below. Further discussion to the approach to financial instruments is set out in Note 1 (Significant accounting policies) and in Note 12.

Currency risk

All of the Company's assets and liabilities are denominated in Pound Sterling and therefore there is no foreign currency risk.

Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates set under a different basis 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 uses interest rate swaps to mitigate any residual interest rate risk.

Credit risk

The principal credit risk to the Company is that the borrowers will not be able to meet their obligations as they fall due. The mortgage loans are secured on a number of UK commercial properties which are geographically diverse and include a diverse tenant portfolio.

Credit risk on the mortgage loans arises where the mortgage loans are secured on underlying commercial properties. The maximum exposure to credit risk is the Statement of Financial Position amount. The largest single exposure to credit risk is the Mapeley Gamma mortgage loan totalling £108,902,614 net of provisions (2015: £139,171,974). This gives rise to a relatively high concentration risk of 83% (2015: 84%) as at year end. The Company monitors the performance of the loans on a regular basis and appoints third party specialist servicers, where required, to help maximise recoveries in the event of breaches or defaults on the loans. Solutus Advisors Ltd is the Special Servicer of the Mapeley Gamma properties.

Impairment

The Company assesses at each reporting date whether there is any objective evidence that a financial asset is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset. The impairment represents the estimated difference between the market valuation of the collateral and the loan outstanding.

DECO 11 – UK CONDUIT 3 PLC

STRATEGIC REPORT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES (CONTINUED)

Impairment (continued)

Mapeley Gamma loan: The loan was placed into special servicing in October 2012 due to a breach of the LTV covenant. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 31 March 2016 by the special servicer and the impairment recognised as at 31 December 2015 was £77,189,085. The special servicer has appointed an asset manager to implement and complete a business plan to enhance the value of the portfolio of properties over a three-year period. An impairment charge of £30,269,359 (2015: reversal of £28,328,539) was recognised during the year, based on the estimated market value of the collateral at 31 December 2016 of £108,902,614 (2015: £139,171,974) and loan principal of £216,361,058 (2015: £216,361,058), resulting in an accumulated impairment provision recognised at 31 December 2016 of £107,458,444 (2015: £77,189,085). The estimated market value is derived by indexing the latest property valuation.

Investco Estate Limited loan: The loan defaulted on its 21 October 2013 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 16 February 2016 by the special servicer. The special servicer continues to market the asset and use the cash received excess of interest to amortise the loan until such time the property is sold. The special servicer's current strategy is disposing the asset through a consensual sale in the second quarter of 2017. An impairment reversal of £54,500 (2015: charge of £209,358) was recognised during the year, based on the estimated market value of the collateral at 31 December 2016 of £961,000 (2015: £1,018,500) and loan principal of £1,323,000 (2015: £1,435,000), resulting in an accumulated impairment provision recognised at 31 December 2016 of £362,000 (2015: £416,500). The estimated market value is derived by indexing the latest property valuation.

Wildmoor Northpoint Limited loan: The loan defaulted on its 25 July 2010 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 31 October 2016 by the special servicer and the balance of impairment at 31 December 2015 was £17,131,045. An impairment charge of £2,971,046 (2015: £1,514,292) was recognised during the year, based on the market value of £16,992,000 (2015: £19,987,733) and loan principal of £37,094,091 (2015: £37,118,778), resulting in an accumulated impairment provision recognised at 31 December 2016 of £20,102,091 (2015: £17,131,045).

CPI Retail Active Management loan: The loan defaulted on its 20 July 2011 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 25 May 2017. An impairment charge of £1,230,038 (2015: £636,628) was recognised during the year, based on the estimated market value of £4,800,000 (2015: £6,030,038) and a loan principal of £7,185,283 (2015: £7,185,283), resulting in an accumulated impairment provision recognised at 31 December 2016 of £2,385,283 (2015: £1,155,245). The estimated market value is derived by indexing the latest property valuation at year end.

As at 31 December 2016, the carrying amount of the mortgage loans amounted to £131,655,615 (gross mortgage loan amount of £261,963,433, with accumulated impairment amounting to £130,307,818 (49.74% of the remaining mortgage loans). The interest income was determined by applying the original effective interest rate to the discounted value of the cash flows with respect to the impaired mortgage loans that are expected to be recoverable. The impaired interest income amounted to £5,089,825 (2015: £nil).

Refinancing risk

The ability of a borrower to make timely payment of principal due on any loan on the relevant loan maturity date may be dependent upon that borrower's ability to refinance the loan. In the event a borrower cannot refinance before or at the loan maturity date, repayment may be delayed, and in some circumstances the collateral, which could be enforced and sold, may be sold at a value below the then outstanding principal of the loan. As a result, repayment of the loan may be made at below par and the Company would be unable to repay certain classes of the loan notes in full.

In the event of the loan notes not being able to be repaid, the loan notes would be written down starting from the lowest class of note, F, to the highest class of note, A-1A.

DECO 11 – UK CONDUIT 3 PLC

STRATEGIC REPORT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT POLICIES (CONTINUED)

Liquidity risk

A facility provided by Danske Bank A/S (London Branch) has been established which will be available, subject to certain criteria and circumstances, in the event of the Company being unable, on a temporary basis, to meet its financial commitments. On 18 November 2016, the liquidity facility for £18,499,718 was renewed for the period from 9 December 2016 to 7 December 2017. The directors expect this facility to be renewed annually.

In 2012, Danske Bank A/S (London Branch) was downgraded below the Requisite Rating and, as per the Liquidity Facility Agreement, a Stand-by Drawing amounting to the full amount of the available facility was drawn down. During the year ended 31 December 2015, £18,512,438 was repaid in full given the improvement in the rating of Danske Bank A/S (London Branch). Further discussion of the Company's approach to financial instruments is set out in note 1 (significant accounting policies) and in note 12.

Corporate governance

The directors have been charged with governance in accordance with the transaction documents describing the structure and operation of the transaction. The governance structure of the Company is such that the key policies have been predetermined at the time of 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 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 disclosure requirements of The Irish Corporate Governance Annex and the provisions of the UK Corporate Governance Code.

Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out above. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. In addition, notes 1 and 12 to the financial statements, include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; and its exposures to credit risk and liquidity risk.

The Company has net liabilities of £140,345,967 (2015: £113,454,793) as a result of accumulated impairments of £130,307,818 (2015: £95,891,874) on the loan assets and derivative liabilities of £657,761 (2015: £9,274,903) held at fair value. However, the terms of the loan notes are limited recourse and therefore the Company is only obliged to repay the notes to the extent that the Company receives cash from the loan assets. The note holders will therefore ultimately bear the Company's deficits on maturity of the notes.

DECO 11 – UK CONDUIT 3 PLC

STRATEGIC REPORT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

Going concern (continued)

Due to the limited recourse nature of the loan notes, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. However, as at 31 December 2016, with the exception of Mapeley Gamma, the loans are past due and will be repaid as soon as the special servicer can dispose of the underlying collateral. The Mapeley Gamma loan has a due date of less than 12 months and is already in special servicing. The special servicer has appointed an asset manager to implement and complete a business plan to enhance the value of the portfolio of properties over a three-year period. As such, the special servicer has no active intention to sell the underlying properties but this remains one of the options available to the special servicer and so the timing of the eventual sale remains uncertain. Once the servicer sells the underlying collaterals the loans will be repaid, the result of which would be that the Company would cease to trade. These conditions indicate the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern. Having considered all the information available to them including the limited recourse nature of the notes, notwithstanding the uncertainty described above, the directors have continued to adopt the going concern basis in preparing the financial statements. The financial statements do not include the adjustments that would result if the Company was unable to continue as a going concern.

Signed on behalf of the Board


for and on behalf of Deco 11 – UK Conduit 3 Plc

Graham Cox

Director
.....18/07/.. 2017

DECO 11 – UK CONDUIT 3 PLC

DIRECTORS' REPORT

FOR THE YEAR ENDED 31 DECEMBER 2016

The directors have pleasure in presenting their report and the audited financial statements of the Deco 11 – UK Conduit 3 Plc (the "Company") for the year ended 31 December 2016.

PRINCIPAL ACTIVITIES

The Company is a special purpose company established in order to issue floating rate loan notes due January 2020 ("the loan notes"), to acquire the beneficial interest in a mortgage portfolio from Deutsche Bank AG, London Branch, ("the mortgage loans"), to open accounts, to create security and receive interest in respect thereof, and to enter into certain related transactions as described in the Offering Circular dated 19 December 2006. On 20 December 2006, the Company issued £444,387,935 loan notes in accordance with the Offering Circular.

RESULTS AND DIVIDENDS

The trading results for the year and the Company's financial position at the end of the year are shown in the attached financial statements.

The Company's loss for the year after tax amounted to £26,891,174 (2015: profit of £35,468,736) after the profit on the financial derivative instrument of £8,617,142 (2015: £9,417,431) and loan impairment charge of £29,326,119 (2015: impairment reversal of £28,210,831). The directors have not recommended a dividend (2015: £nil).

CREDITOR PAYMENT POLICY

The Company's policy concerning payment of its trade creditors is to pay in accordance with its contractual and other legal obligations. Due to the nature of the business, the main creditors are the noteholders. Principal and interest is repaid quarterly in accordance with the agreements in place. The Company does not follow any other code or standard on payment practice.

DIRECTORS

The directors, who served the Company during the year, were as follows:

Mr Graham Cox
Mr Graham Hodgkin

AUDITOR

Deloitte LLP have expressed their willingness to continue in office as auditor and a resolution to re-appoint them as auditor for the ensuing year will be proposed at the next annual general meeting.

DECO 11 – UK CONDUIT 3 PLC

DIRECTORS' REPORT (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

STATEMENT OF DISCLOSURE OF INFORMATION TO THE AUDITOR

The directors confirm that:

- so far as the directors are aware, there is no relevant audit information of which the Company's auditor is unaware; and
- each of the directors have taken all steps that they ought to have as directors in order to make themselves aware of any relevant audit information and to establish that the Company's auditor is aware of that information.

This confirmation is given and should be interpreted in accordance with the provisions of s418 of the Companies Act 2006.

Signed on behalf of the Board

Director


Graham Cox

18/07/2017

DECO 11 – UK CONDUIT 3 PLC

DIRECTORS' RESPONSIBILITIES STATEMENT

FOR THE YEAR ENDED 31 DECEMBER 2016

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

Company law requires the directors to prepare financial statements for each financial year. Under that law the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRSs) as adopted by the European Union. Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that year. In preparing these financial statements, International Accounting Standard 1 requires that directors:

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

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

Signed on behalf of the Board

Director *Graham Cox*

18/07/ 2017

DECO 11 – UK CONDUIT 3 PLC

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DECO 11 – UK CONDUIT 3 PLC

We have audited the financial statements of Deco 11 – UK Conduit 3 Plc for the year ended 31 December 2016 which comprise the Statement of Comprehensive Income, the Statement of Financial Position, the Statement of Changes in Equity, the Statement of Cash Flows and the related notes 1 to 16. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the European Union.

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.

Respective responsibilities of directors and auditor

As explained more fully in the Directors' Responsibilities Statement, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view. Our responsibility is to audit and express an opinion on the financial statements in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the financial statements

An audit involves obtaining evidence about the amounts and disclosures in the financial statements sufficient to give reasonable assurance that the financial statements are free from material misstatement, whether caused by fraud or error. This includes an assessment of: whether the accounting policies are appropriate to the Company's circumstances and have been consistently applied and adequately disclosed; the reasonableness of significant accounting estimates made by the directors; and the overall presentation of the financial statements. In addition, we read all the financial and non-financial information in the annual report to identify material inconsistencies with the audited financial statements and to identify any information that is apparently materially incorrect based on, or materially inconsistent with, the knowledge acquired by us in the course of performing the audit. If we become aware of any apparent material misstatements or inconsistencies we consider the implications for our report.

Opinion on financial statements

In our opinion the financial statements:

- give a true and fair view of the state of the Company's affairs as at 31 December 2016 and of its loss for the year then ended;
- have been properly prepared in accordance with IFRSs as adopted by the European Union; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Emphasis of matter – going concern

In forming our opinion on the financial statements, which is not modified, we have considered the adequacy of disclosure made in note 1 to the financial statements concerning the Company's ability to continue as a going concern. The Mapeley Gamma loan has a due date of less than 12 months but is already in special servicing. There is no active intention to sell the underlying properties but this remains one of the options available to the special servicer and so the timing of the eventual sale remains uncertain. These conditions, along with the other matters explained in note 1 to the financial statements indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. The financial statements do not include the adjustments that would result if the Company was unable to continue as a going concern.

INDEPENDENT AUDITOR'S REPORT TO THE MEMBERS OF DECO 11 – UK CONDUIT 3 PLC (continued)

Opinion on other matters prescribed by the Companies Act 2006

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

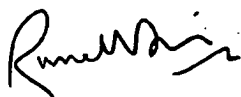
- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and the Directors' Report have been prepared in accordance with applicable legal requirements.

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified any material misstatements in the Strategic Report and the Directors' Report.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.



Russell Davis, FCA, (Senior Statutory Auditor)
for and on behalf of Deloitte LLP
Statutory Auditor
London, United Kingdom

18 July 2017

DECO 11 – UK CONDUIT 3 PLC

STATEMENT OF COMPREHENSIVE INCOME

FOR THE YEAR ENDED 31 DECEMBER 2016

Continuing operations	Notes	2016 £	2015 £
Interest income	2	7,538,619	14,977,194
Interest expense	3	<u>(12,260,510)</u>	<u>(12,760,733)</u>
Net interest (expense)/income		<u>(4,721,891)</u>	<u>2,216,461</u>
Impairment (charge)/reversal of commercial mortgage loans	6	(29,326,119)	28,210,831
Mortgage loans written off	6	-	(2,161,991)
Fair value gain on derivative financial instruments	13	8,617,142	9,417,431
Other operating expenses	4	<u>(1,460,053)</u>	<u>(2,213,697)</u>
		<u>(22,169,030)</u>	<u>33,252,574</u>
(Loss)/profit before tax for the year		(26,890,921)	35,469,035
Income tax charge	5	<u>(253)</u>	<u>(299)</u>
Total (loss)/profit after tax		(26,891,174)	35,468,736
Other comprehensive income		-	-
Total comprehensive (loss)/income for the year		<u>(26,891,174)</u>	<u>35,468,736</u>

The notes on pages 16 to 33 form part of these financial statements.

DECO 11 – UK CONDUIT 3 PLC

STATEMENT OF FINANCIAL POSITION

AS AT 31 DECEMBER 2016

	Notes	2016 £	2015 £
Assets			
Non-current assets			
Mortgage loans	6	-	139,171,974
Current assets			
Mortgage loans	6	131,655,615	27,036,272
Trade and other receivables	7	1,419,282	3,021,820
Cash and cash equivalents	8	56,984	55,319
		<u>133,131,881</u>	<u>30,113,411</u>
Total assets		<u>133,131,881</u>	<u>169,285,385</u>
Equity			
Share capital	9	12,502	12,502
Retained losses	9	(140,358,469)	(113,467,295)
Total shareholders' deficit	9	<u>(140,345,967)</u>	<u>(113,454,793)</u>
Non-current liabilities			
Loan notes	10	138,654,079	243,410,109
Total non-current liabilities		<u>138,654,079</u>	<u>243,410,109</u>
Current liabilities			
Loan notes	10	131,655,615	27,036,272
Interest payable on loan notes	10	521,908	433,911
Trade and other payables	11	1,988,485	2,584,983
Derivative financial instruments	13	657,761	9,274,903
Total current liabilities		<u>134,823,769</u>	<u>39,330,069</u>
Total liabilities		<u>273,477,848</u>	<u>282,740,178</u>
Total equity and liabilities		<u>133,131,881</u>	<u>169,285,385</u>

These financial statements of Deco 11 – UK Conduit 3 Plc, Company Registration 5990966 on pages 12 to 33 were approved and authorised for issue by the directors on 18/07/2017 and are signed on their behalf by:

Director

Graham Cox

The notes on pages 16 to 33 form part of these financial statements.

DECO 11 – UK CONDUIT 3 PLC**STATEMENT OF CHANGES IN EQUITY****FOR THE YEAR ENDED 31 DECEMBER 2016**

	Share capital £	Retained losses £	Total equity £
Balance as at 1 January 2015	12,502	(148,936,031)	(148,923,529)
Profit for the year 31 December 2015	-	35,468,736	35,468,736
Other comprehensive income for the year	-	-	-
Balance at 31 December 2015	<u>12,502</u>	<u>(113,467,295)</u>	<u>(113,454,793)</u>

	Share capital £	Retained losses £	Total equity £
Balance as at 1 January 2016	12,502	(113,467,295)	(113,454,793)
Loss for the year 31 December 2016	-	(26,891,174)	(26,891,174)
Other comprehensive income for the year	-	-	-
Balance at 31 December 2016	<u>12,502</u>	<u>(140,358,469)</u>	<u>(140,345,967)</u>

The notes on pages 16 to 33 form part of these financial statements.

DECO 11 – UK CONDUIT 3 PLC

STATEMENT OF CASH FLOWS

FOR THE YEAR ENDED 31 DECEMBER 2016

	Notes	2016 £	2015 £
Operating activities			
(Loss)/profit before tax for the year		(26,890,921)	35,469,035
<i>Adjustments for:</i>			
Fair value movement on derivative financial instruments		(8,617,142)	(9,417,431)
Impairment charge/(reversal) on commercial mortgage loans	6	34,415,944	(28,210,831)
Mortgage loans written off		-	2,161,991
Bank interest received		(255)	(43,613)
Decrease/(increase) in trade and other receivables		1,602,538	(376,476)
(Decrease)/increase in trade and other payables		(508,450)	388,431
Tax paid		(304)	(791)
Net cash generated from/(used in) operating activities		<u>1,410</u>	<u>(29,685)</u>
Investing activities			
Bank interest received		255	43,613
Movement on funds placed on deposit		-	18,460,970
Repayments of mortgage loans	6	<u>136,687</u>	<u>10,002,154</u>
Net cash from investing activities		<u>136,942</u>	<u>28,506,737</u>
Financing activities			
Liquidity facility movement		-	(18,512,438)
Repayments of loan notes	10	<u>(136,687)</u>	<u>(10,002,154)</u>
Net cash used in financing activities		<u>(136,687)</u>	<u>(28,514,592)</u>
Net increase/(decrease) in cash and cash equivalents		1,665	(37,540)
Cash and cash equivalents at beginning of year		<u>55,319</u>	<u>92,859</u>
Cash and cash equivalents at 31 December	8	<u>56,984</u>	<u>55,319</u>

Actual cash received and paid as interest income on the mortgage loans and interest expense on the loan notes (excluding class X interest) during the year was £13,826,840 (2015: £14,961,045) and £2,246,668 (2015: £2,447,353) respectively.

As explained in the accounting policies on page 19, the cash is not freely available to be used.

The notes on pages 16 to 33 form part of these financial statements.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS

FOR THE YEAR ENDED 31 DECEMBER 2016

1. SIGNIFICANT ACCOUNTING POLICIES

Deco 11 – UK Conduit 3 Plc is a Company incorporated in the United Kingdom under the Companies Act 2006 and domiciled in England.

Statement of compliance

The Company's financial statements have been prepared in accordance with International Financial Reporting Standards as adopted by the European Union ("IFRSs") as they apply to the financial statements of the Company for the year ended 31 December 2016.

The accounting policies set out below have been applied in respect of the financial year ended 31 December 2016.

Basis of preparation

The financial statements have been prepared on the historical cost basis as modified for the revaluation of certain financial instruments under IAS 39 Financial Instruments: Recognition and Measurement.

The financial statements are presented in Pound Sterling.

Due to the fact that the nature of the business is to provide finance, the directors are of the opinion that it is more appropriate to use interest income and interest expense rather than turnover and cost of sales in preparing the Statement of Comprehensive Income.

Going concern

The Company's business activities, together with the factors likely to affect its future development, performance and position are set out in the strategic and directors' report. The financial position of the Company, its cash flows, liquidity position and borrowing facilities are set out in the financial statements. In addition, notes 1 and 12 to the financial statements, include the Company's objectives, policies and processes for managing its capital; its financial risk management objectives; and its exposures to credit risk and liquidity risk.

The Company has net liabilities of £140,345,967 (2015: £113,454,793) as a result of accumulated impairments of £130,307,818 (2015: £95,891,874) on the loan assets and derivative liabilities of £657,761 (2015: £9,274,903) held at fair value. However, the terms of the loan notes are limited recourse and therefore the Company is only obliged to repay the notes to the extent that the Company receives cash from the loan assets. The note holders will therefore ultimately bear the Company's deficits on maturity of the notes.

Due to the limited recourse nature of the loan notes, the directors have a reasonable expectation that the Company has adequate resources to continue in operational existence for the foreseeable future. However, as at 31 December 2016, with the exception of Mapeley Gamma, the loans are past due and will be repaid as soon as the special servicer can dispose of the underlying collateral. The Mapeley Gamma loan has a due date of less than 12 months and is already in special servicing. The special servicer has appointed an asset manager to implement and complete a business plan to enhance the value of the portfolio of properties over a three-year period. There is no active intention to sell the underlying properties but this remains one of the options available to the special servicer and so the timing of the eventual sale remains uncertain. Once the servicer sells the underlying collaterals the loans will be repaid, the result of which would be that the Company would cease to trade. These conditions, along with other matters explained in note 1 to the financial statements indicate the existence of a material uncertainty which may cast significant doubt about the Company's ability to continue as a going concern. Having considered all the information available to them including the limited recourse nature of the notes, notwithstanding the uncertainty described above, the directors have continued to adopt the going concern basis in preparing the financial statements. The financial statements do not include the adjustments that would result if the Company was unable to continue as a going concern.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Critical accounting judgements and key sources of estimation uncertainty

The preparation of financial statements in conformity with IFRSs requires management to make judgements, estimates and assumptions that affect the application of policies and reported amounts of assets and liabilities, income and expenses. In particular, for the fair value of derivatives (note 13) and the recoverability of assets (note 6), the estimates and associated assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making judgements and carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates used in the financial statements.

The estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the year in which the estimate is revised if the revision affects only that year or in the year of the revision and future years if the revision affects both the current and future years.

Financial instruments

The Company's financial instruments comprise mortgage loans, cash and cash equivalents, derivatives, loan notes and various receivables and payables that arise directly from its operations. The main purpose of the loan notes is to finance the beneficial interest in a mortgage portfolio. These financial instruments are classified in accordance with the principles of IAS 39 Financial Instruments: Recognition and Measurement as described below.

Mortgage loans

The mortgage loans are classified as loans and receivables and are initially measured at fair value with subsequent measurement being at amortised cost using the effective interest method.

Impairment

Appropriate allowances for estimated irrecoverable amounts are recognised in profit or loss when there is objective evidence that the asset is impaired. The allowance is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the effective interest rate computed at initial recognition.

The Company assesses at each statement of financial position date whether, as a result of one or more events that occurred after initial recognition, there is objective evidence that a financial asset or group of financial assets is impaired. Evidence of impairment may include:

- i) indications that the borrower or group of borrowers is experiencing significant financial difficulty
- ii) default or delinquency in interest or principal payments
- iii) debt being restructured to reduce the burden on the borrower.

The Company first assesses whether objective evidence of impairment exists either individually for assets that are separately significant or individually or collectively for assets that are not separately significant. If there is no objective evidence of impairment for an individually assessed asset, then no impairment assessment is performed.

If there is objective evidence that an impairment loss has been incurred, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate. The resultant provisions are deducted from the appropriate asset values in the statement of financial position.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Impairment (continued)

The methodology and assumptions used for estimating future cash flows are reviewed regularly by the Directors to reduce any differences between loss estimates and actual loss experience.

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognised, the provision is adjusted and the amount of the reversal is recognised in the income statement.

Loans remain on the statement of financial position net of associated provisions until they are deemed no longer recoverable. Where a loan is not recoverable, it is written off against the related provision for loan impairment once all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the income statement.

Commercial loans

In assessing objective evidence of a loss event for commercial loans, the following key indicators are considered:

- i) high loan to value
- ii) covenant breaches
- iii) loss of significant tenants or other decreases in tenant quality
- iv) the probability of the borrower entering bankruptcy
- v) local economic conditions (for example, where this impacts on the value of underlying collateral).

Where there is objective evidence of impairment, we assess cash flows on a case by case basis considering the following factors:

- i) our exposure to the borrower
- ii) the viability of the borrowers' business model and their capacity to trade successfully out of financial difficulties and generate sufficient cash flow to service debt obligations
- iii) the amount and timing of expected receipts and recoveries of collateral
- iv) the extent of other creditors' claims ranking ahead of the Company's, and the likelihood of other creditors continuing to support the borrower
- v) the complexity of determining the aggregate amount and ranking of all creditor claims and the extent to which legal and insurance uncertainties are evident
- vi) the realisable value of security at the expected date of sale and likelihood of successful repossession
- vii) the likely deduction of any costs involved in recovery of amounts outstanding.

De-recognition of financial assets

The Company derecognises a financial asset only when the contractual rights to the cash flows from the asset expire; or it transfers the financial asset and substantially all the risks and rewards of ownership of the asset to another entity. If the Company neither transfers nor retains substantially all the risks and rewards of ownership and continues to control the transferred asset, the Company recognises its retained interest in the asset and an associated liability for amounts it may have to pay. If the Company retains substantially all the risks and rewards of ownership of a transferred financial asset, the Company continues to recognise the financial asset and also recognises a collateralised borrowing for the proceeds received.

Deferred consideration

A deferred consideration charge/(release) is included in interest expense. Deferred consideration is payable to the Class X certificate holders, dependent on the extent to which the surplus income, in excess of the agreed margin, generated by the mortgage loans in which the Company has purchased an interest, exceeds the administration costs of the mortgage loans.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

Cash and cash equivalents

Cash and cash equivalents in the Statement of Financial Position comprise cash at banks and short-term deposits with an original maturity of three months or less. All withdrawals from the Company's bank accounts are restricted by the detailed priority of payments set out in the securitisation agreements and as such the cash and cash equivalents are not freely available to be used for other purposes.

Derivative financial instruments and hedging activities

The Company uses derivative financial instruments to hedge its exposure to interest rate risk arising from operational, financing and investment activities. In accordance with its treasury policy, the Company does not hold or issue derivative financial instruments for trading purposes. Derivatives are accounted for as held for trading.

IAS 39 requires all financial assets and liabilities to be recognised initially at fair value on the Statement of Financial Position. Subsequent to initial recognition, any changes in fair value of the derivatives held are recognised in the Statement of Comprehensive Income.

The fair value of interest rate swaps and basis swaps is the estimated amount that the Company would receive or pay to terminate the swap at the reporting date, taking into account current interest rates and the current creditworthiness of the swap counterparties.

Loan notes

Loan notes are classified as other financial liabilities and recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, loan notes are stated 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 effective interest basis.

Embedded derivatives

Certain derivatives are embedded within other non-derivative host financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risks of the host instrument, and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivatives recognised in the Statement of Comprehensive Income. Depending on the classification of the host instrument, the host is then measured in accordance with IAS 39.

Interest income and expense

Interest income and expense is accounted for on a time basis, by reference to the principal outstanding and at the effective interest rate applicable, which is the rate that exactly discounts estimated future cash receipts or payments through the expected life of the financial asset or liability to that asset's or liability's net carrying amount.

Value added tax

Value added tax is not recoverable by the Company and is included within its related cost.

Income tax expense

Income tax in the Statement of Comprehensive Income for the year comprises current and deferred tax. Income tax is recognised as expense or gain except to the extent that it relates to items recognised directly in other comprehensive income, in which case it is recognised in other comprehensive income.

Income tax expense is calculated by reference to the profit of the Company which is required to be retained in accordance with the pre-enforcement priority of payments as defined in the terms and conditions of the loan notes. Further information is disclosed in note 5.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

1. SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

New and amended standards effective and adopted during the year

All new and amended accounting standards which have become effective for the current year have been adopted but have had no material effect on the reported performance, financial position or disclosures of the Company, therefore these standards have not been listed separately.

New and amended standards issued, not yet effective and not early adopted

At the date of authorisation of these financial statements, the following Standards and Interpretations which have not been applied in these financial statements were in issue but not yet effective and in some cases have not been adopted by EU:

- IFRS 15 Revenue from Contracts with Customers
- IFRS 9 Financial Instruments
- IFRS 16 Leases
- Disclosure Initiative (Amendments to IAS 7: Statement of cash flows)

The directors do not expect that the adoption of the Standards and Interpretations listed above will have a material impact on the financial statements of the Company in future periods, except for IFRS 9 which will impact both the measurement and disclosures of financial instruments.

Beyond the information above, it is not practicable to provide a reasonable estimate of the effect of these standards until a detailed review has been completed.

Segmental reporting

The principal asset of the Company is the beneficial interest in the mortgage portfolio originated in the United Kingdom which is funded by loan notes issued in the United Kingdom. The directors do not consider it necessary to provide a further analysis of the results of the Company from those already disclosed in these financial statements because there is only one segment.

2. INTEREST INCOME

	2016	2015
	£	£
Income from mortgage loans	7,538,364	14,933,581
Bank interest income	255	43,613
	<u>7,538,619</u>	<u>14,977,194</u>

3. INTEREST EXPENSE

	2016	2015
	£	£
Interest on loan notes	2,334,666	2,437,473
Net swap interest payable	9,074,859	8,848,338
Deferred consideration	850,985	1,418,586
Bank interest paid	-	56,336
	<u>12,260,510</u>	<u>12,760,733</u>

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

4. OTHER OPERATING EXPENSES

	2016	2015
	£	£
Fees for the audit of the Company's annual accounts	24,600	24,600
Fees payable to the auditor for tax services	9,540	9,270
Administration and cash management fees	1,166,611	1,798,208
Corporate services fee	16,693	13,427
Accountancy fee	34,504	7,429
Legal and professional fees	140,429	305,593
Other expenses	67,676	55,170
	<u>1,460,053</u>	<u>2,213,697</u>

Directors' emoluments during the year amounted to £4,800 (2015: £4,800), being £2,400 (2015: £2,400) each, for their services as directors to the Company during the year with £nil (2015: £nil) unpaid at year end. The directors had no material interest in any contract of significance in relation to the business of the Company (2015: none). The Company did not have any employees in the current year (2015: none).

5. INCOME TAX CHARGE

The Company has elected to be taxed under the Taxation of Securitisation Companies 2006 (Regulations) i.e. the "permanent regime". Corporation tax is therefore calculated by reference to the profit of the Company which is required to be retained in accordance with the pre-enforcement priority of payments as defined in the terms and conditions of the loan notes.

The directors are satisfied that the Company meets the definition of a 'securitisation company' as defined by both The Finance Act 2005 and the subsequent secondary legislation and that no incremental unfunded tax liabilities will arise.

	2016	2015
	£	£
Current tax:		
Corporation tax charge for the year at a rate of 20% (2015: 20%)	<u>253</u>	<u>299</u>
Total income tax charge in Statement of Comprehensive Income	<u>253</u>	<u>299</u>
Reconciliation of total tax charge	£	£
(Loss)/Profit before tax	<u>(26,890,921)</u>	<u>35,469,035</u>
(Loss)/Profit before tax multiplied by the standard rate of corporation tax in the UK of 20% (2015: 20%)	<u>(5,378,184)</u>	<u>7,093,807</u>
Permanent differences relating to application of Taxation of Securitisation Companies Regulations 2006	<u>5,378,437</u>	<u>(7,093,508)</u>
Total tax charge reported in the Statement of Comprehensive Income	<u>253</u>	<u>299</u>

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

6. MORTGAGE LOANS

	2016 £	2015 £
At 1 January	166,208,246	150,161,560
Redemptions	(136,687)	(10,002,154)
Loan written off	-	(2,161,991)
Movement in the impairment provision during the year	<u>(34,415,944)</u>	<u>28,210,831</u>
At 31 December	<u>131,655,615</u>	<u>166,208,246</u>
The balance can be analysed as follows:		
Current assets	131,655,615	27,036,272
Non-current assets	<u>-</u>	<u>139,171,974</u>
	<u>131,655,615</u>	<u>166,208,246</u>

	2016 £	2015 £
The movement of the impairment provision is as follows:		
At 1 January	(95,891,874)	(124,102,705)
Provisions made during the year	(34,415,944)	-
Reversals during the year	-	28,210,831
At 31 December	<u>(130,307,818)</u>	<u>(95,891,874)</u>

The movement of the impairment provision in the Statement of Comprehensive Income differs from the actual movement of the impairment provision by the impaired interest income adjustment. A reconciliation of the movement of the impairment provision is provided below:

	2016 £	2015 £
Actual (provision)/reversal during the year	(34,415,944)	28,210,831
Impaired interest income adjustment	<u>5,089,825</u>	<u>-</u>
Impairment (charge)/reversal as per Statement of Comprehensive Income	<u>(29,326,119)</u>	<u>28,210,831</u>

As at 31 December 2016, the carrying amount of the mortgage loans amounted to £131,655,615 (gross mortgage loan amount of £261,963,433, with accumulated impairment amounting to £130,307,818 (49.74% of the remaining mortgage loans). The interest income recognised was determined by applying the original effective interest rate to the discounted value of the cash flows with respect to the impaired mortgage loans that are expected to be recoverable. The impaired interest income amounted to £5,089,825 (2015: £nil).

The mortgage loans are classified as “loans and receivables”. The Mapeley Gamma loan is due for repayment in January 2017, whereas all the other loans have defaulted on their maturity date. At 31 December 2016, the floating or fixed rate of interest on the mortgage loans ranged from 1.18% to 5.38% (2015: 1.35% to 5.38%). The mortgage loans are secured over commercial properties. Deutsche Bank AG, London Branch acts as security trustee to the loans.

The Company assesses at each reporting date whether there is any objective evidence that a financial asset is impaired. A financial asset or portfolio of financial assets is impaired and an impairment loss incurred if there is objective evidence that an event or events since initial recognition of the asset have adversely affected the amount or timing of future cash flows from the asset. The impairment represents the estimated difference between the market valuation of the collateral and the loan outstanding.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

6. MORTGAGE LOANS (CONTINUED)

Mapeley Gamma loan: The loan was placed into special servicing in October 2012 due to a breach of the LTV covenant. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 31 March 2016 by the special servicer and the impairment recognised as at 31 December 2015 was £77,189,085. The special servicer has appointed an asset manager to implement and complete a business plan to enhance the value of the portfolio of properties over a three-year period. An impairment charge of £30,269,359 (2015: reversal of £28,328,539) was recognised during the year, based on the estimated market value of the collateral at 31 December 2016 of £108,902,614 (2015: £139,171,974) and loan principal of £216,361,058 (2015: £216,361,058), resulting in an accumulated impairment provision recognised at 31 December 2016 of £107,458,444 (2015: £77,189,085). The estimated market value is derived by indexing the latest property valuation.

Investco Estate Limited loan: The loan defaulted on its 21 October 2013 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 16 February 2016 by the special servicer. The special servicer continues to market the asset and use the cash received excess of interest to amortise the loan until such time the property is sold. The special servicer's current strategy is disposing the asset through a consensual sale in the second quarter of 2017. An impairment reversal of £54,500 (2015: charge of £209,358) was recognised during the year, based on the estimated market value of the collateral at 31 December 2016 of £961,000 (2015: £1,018,500) and loan principal of £1,323,000 (2015: £1,435,000), resulting in an accumulated impairment provision recognised at 31 December 2016 of £362,000 (2015: £416,500). The estimated market value is derived by indexing the latest property valuation.

Wildmoor Northpoint Limited loan: The loan defaulted on its 25 July 2010 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 31 October 2016 by the special servicer and the balance of impairment at 31 December 2015 was £17,131,045. An impairment charge of £2,971,046 (2015: £1,514,292) was recognised during the year, based on the market value of £16,992,000 (2015: £19,987,733) and loan principal of £37,094,091 (2015: £37,118,778), resulting in an accumulated impairment provision recognised at 31 December 2016 of £20,102,091 (2015: £17,131,045).

CPI Retail Active Management loan: The loan defaulted on its 20 July 2011 maturity date and was subsequently placed into special servicing. As such, an impairment assessment is carried out annually on the loan. The property was last valued on 25 May 2017. An impairment charge of £1,230,038 (2015: £636,628) was recognised during the year, based on the estimated market value of £4,800,000 (2015: £6,030,038) and a loan principal of £7,185,283 (2015: £7,185,283), resulting in an accumulated impairment provision recognised at 31 December 2016 of £2,385,283 (2015: £1,155,245). The estimated market value is derived by indexing the latest property valuation at year end.

Key assumptions included in the measurement of impairment include the probability of any account going into default, the probability of defaulted accounts progressing to possession and the eventual loss incurred in the event of forced sale or write off. These assumptions are based on observed historical data and updated as management considers appropriate to reflect current conditions and the Company's strategy for the book. The accuracy of the impairment provision would therefore be affected by unexpected changes in these assumptions.

Sensitivity analysis

A 5% increase/decrease on the sales value of the loan would decrease/ increase the impairment provision by an estimated £849,600.

For commercial mortgages the estimate of housing price index (HPI) movements is also a key assumption in estimating the eventual loss. The Company does not take account of projected future HPI increases in establishing provisions. If future HPI increases do materialise then this will reduce the amount of actual loss incurred. A 5% increase/decrease on the indexed market value of the loan would decrease/increase the impairment provision by an estimated £5,733,181.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

7. TRADE AND OTHER RECEIVABLES

	2016 £	2015 £
Amounts owed by parent undertaking	2,523	2,523
Prepayments and accrued income	1,416,759	2,615,358
Other current assets	-	403,939
	<u>1,419,282</u>	<u>3,021,820</u>

8. CASH AND CASH EQUIVALENTS

	2016 £	2015 £
Cash and cash equivalents	<u>56,984</u>	<u>55,319</u>

The directors consider that the carrying value of cash and cash equivalents approximates to their fair value.

9. TOTAL SHAREHOLDERS' DEFICIT

	Issued capital £	Retained losses £	Total £
At 1 January 2016	12,502	(113,467,295)	(113,454,793)
Loss for the year	-	<u>(26,891,174)</u>	<u>(26,891,174)</u>
Balance at 31 December 2016	<u>12,502</u>	<u>(140,358,469)</u>	<u>(140,345,967)</u>

There are 50,000 authorised ordinary shares of £1 each. The issued share capital comprises two fully paid £1 shares; and 49,998 ordinary shares quarterly paid. Castlewoods CS Holdings Limited holds one fully paid £1 share under a declaration of trust for charitable purposes. The remaining 49,999 shares are held by Deco 11 – UK Conduit 3 Holding Limited.

10. LOAN NOTES

This note provides information about the contractual terms of the Company's loan notes. For more information about the Company's exposure to interest rate risk, see note 12.

	2016 £	2015 £
At 1 January	270,446,381	280,448,535
Redemptions	<u>(136,687)</u>	<u>(10,002,154)</u>
	<u>270,309,694</u>	<u>270,446,381</u>
Non-current liabilities		
Loan notes	<u>138,654,079</u>	<u>243,410,109</u>
	<u>138,654,079</u>	<u>243,410,109</u>
Current liabilities		
Loan notes	131,655,615	27,036,272
Interest payable on loan notes	<u>521,908</u>	<u>433,911</u>
	<u>132,177,523</u>	<u>27,470,183</u>

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled in order of priority in accordance with the Offering Circular.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

10. LOAN NOTES (CONTINUED)

On 20 December 2006, an agreement was entered into with Danske Bank A/S (London Branch) for the provision of a liquidity facility for the Company. The facility is in place to allow the Company to meet its obligations should there be a shortfall in the revenue or principal received from the mortgage loans. At the Statement of Financial Position date, the limit on this facility was £18,499,718 (2015: £18,499,718). A commitment fee of 0.15% per annum is charged on the undrawn amount of the liquidity facility commitment.

An amount of £ nil (2015: £ nil) of liquidity facility was drawn as at 31 December 2016. In 2012, Danske Bank A/S (London Branch) was downgraded below the Requisite Rating and, as per the Liquidity Facility Agreement, a Stand-by Drawing amounting to the full amount of the available facility was drawn down. During the year ended 31 December 2015, £18,512,438 was repaid in full given the improvement in the rating of Danske Bank A/S (London Branch). Further discussion of the Company's approach to financial instruments is set out in note 1 (significant accounting policies) and in note 12.

On 20 December 2006, the Company issued the following class of Notes:

Class of Notes	Currency	Issue price	Interest	Margin	Maturity
A-1A	GBP	220,000,000	3 month Libor	0.19%	January 2020
A-1B	GBP	74,500,000	3 month Libor	0.23%	January 2020
A-2	GBP	45,500,000	3 month Libor	0.25%	January 2020
B	GBP	27,000,000	3 month Libor	0.33%	January 2020
C	GBP	37,000,000	3 month Libor	0.50%	January 2020
D	GBP	29,000,000	3 month Libor	0.85%	January 2020
E	GBP	6,000,000	3 month Libor	1.25%	January 2020
F	GBP	5,387,935	3 month Libor	3.40%	January 2020

At the reporting date, the outstanding amount for each class of Notes were as shown in table below:

Class of Notes	2016	2015
	£	£
A-1A	54,560,595	54,697,282
A-1B	70,742,442	70,742,442
A-2	43,205,116	43,205,116
B	26,191,835	26,191,835
C	36,124,333	36,124,333
D	28,229,956	28,229,956
E	5,920,596	5,920,596
F	<u>5,334,821</u>	<u>5,334,821</u>
	<u>270,309,694</u>	<u>270,446,381</u>

11. TRADE AND OTHER PAYABLES

	2016	2015
	£	£
Current liabilities		
Accruals and deferred income	1,944,400	2,584,983
Deferred consideration	<u>44,085</u>	-
	<u>1,988,485</u>	<u>2,584,983</u>

Current liabilities due within one year are paid when cash is available after other commitments have been fulfilled, in order of priority in accordance with the Offering Circular.

The directors consider that the carrying amount of trade and other payables approximates to their fair value.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT

The principal risks and uncertainties are set out in the Strategic Report on pages 2 to 6.

Financial instruments

The Company's financial instruments, other than derivatives, comprise mortgage loans, cash and cash equivalents, loan notes and various receivables and payables that arise directly from its operations. The Company also enters into derivative transactions (principally interest rate swaps). The purpose of such transactions is to manage the interest rate risks arising from the Company's operations and its sources of finance.

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

The directors have considered the financial risks affecting the Company and have included the relevant disclosures of interest rate, credit, liquidity and currency risks in the Strategic Report.

Fair values, methodology and assumptions

Fair values

Fair value is defined as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date (i.e. an exit price). The fair value of financial instruments is always determined on the basis of the listed price on an active market (mark to market) or, if this is not possible, on the basis of industry standard valuation models (mark to matrix or mark to model).

Financial instruments valued using observable market prices

If a quoted market price in an active market is available for an instrument, the fair value is calculated based on the market price.

Financial instruments valued using a valuation technique

In the absence of a quoted market price in an active market, management uses industry standard models to make its best estimate of the price that the market would set for that financial instrument. In order to make these estimations, various techniques are employed, including extrapolation from observable market data and observation of similar financial instruments with similar characteristics. Wherever possible, valuation parameters for each product are based on prices directly observable in active markets or that can be derived from directly observable market prices.

The Company did not make any material changes to the valuation techniques and industry standard models it used during the year ended 31 December 2016.

Fair value hierarchy

The Company applies the following fair value hierarchy that prioritises the inputs to valuation techniques used in measuring fair value. The hierarchy establishes three categories for valuing financial instruments, giving the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

Level 1 - Unadjusted quoted prices for identical assets or liabilities in an active market that the Company has the ability to access at the measurement date.

Level 2 - Quoted prices in markets that are not active, quoted prices for similar assets or liabilities, recent market transactions, inputs other than quoted market prices for the asset or liability that are observable either directly or indirectly for substantially the full term, and inputs to valuation techniques that are derived principally from or corroborated by observable market data through correlation or other statistical means for substantially the full term of the asset or liability.

Level 3 - Inputs to the pricing or valuation techniques that are significant to the overall fair value measurement of the asset or liability are unobservable.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Fair value hierarchy (Continued)

The methodology and assumptions used in estimating the fair value of financial instruments are disclosed below. The only financial instruments held at fair value on the Statement of Financial Position are derivatives. All the derivatives fall within the level 2 fair value hierarchy.

The fair value of the derivatives held by the Company is calculated using the Overnight Indexed Swap (OIS) methodology which are based on significant observable inputs. For OIS methodology, discounting is calibrated to the rates structure of the prevailing market interest rate where the derivatives are originated, that is, United Kingdom. Therefore, the Sterling Overnight Interbank Average Rate (SONIA), an index that tracks Sterling Overnight funding rates, is used.

The fair values together with the carrying amounts shown in the Statement in Financial Position are as follows:

	Notes	Carrying amount 2016 £	Fair value 2016 £	Carrying amount 2015 £	Fair value 2015 £
Mortgage loans	6	131,655,615	138,841,817	166,208,246	150,872,577
Trade and other receivables	7	1,419,282	1,419,282	3,021,820	3,021,820
Cash and cash equivalents	8	56,984	56,984	55,319	55,319
		<u>133,131,881</u>	<u>140,318,083</u>	<u>169,285,385</u>	<u>153,949,716</u>
Derivative financial instruments	13	657,761	657,761	9,274,903	9,274,903
Loan notes	10	270,309,694	138,184,055	270,446,381	140,007,150
Interest payable on loan notes	10	521,908	521,908	433,911	433,911
Trade and other payables	11	1,988,485	1,988,485	2,584,983	2,584,983
		<u>273,477,848</u>	<u>141,352,209</u>	<u>282,740,178</u>	<u>152,300,947</u>

The fair value of the loan notes is based on observable inputs given that these notes are listed on the Irish Stock Exchange and hence a market price is available for each class of loan notes excluding the Class E and F notes. For those classes of notes for which a market price is not available, a fair value of £nil was used. However, given that the loan notes are thinly traded, the market price is manually adjusted for large moves, backwardation and general price challenges received. Therefore the loan notes have been categorised as level 2 financial instruments.

The fair value of mortgage loans are based on fair value of loan notes and derivatives that wherever possible have been estimated using quoted market prices for instruments held. Hence the mortgage loans have been deemed to a level 2 instruments as well. The carrying values of cash and cash equivalents, trade and other receivables, interest payable, trade and other payables and current tax liability are a reasonable approximation of the fair values of these instruments.

Financial instruments recognised and measured at fair value

As at 31 December 2016	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Liabilities				
Derivative financial instruments	<u>(657,761)</u>	<u>-</u>	<u>(657,761)</u>	<u>-</u>

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Fair value hierarchy (Continued)

Financial instruments at amortised cost whose fair value is disclosed

As at 31 December 2016	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Assets				
Mortgage loans	<u>138,841,817</u>	<u>-</u>	<u>138,841,817</u>	<u>-</u>
Liabilities				
Loan notes	<u>(138,184,055)</u>	<u>-</u>	<u>(138,084,055)</u>	<u>-</u>

Financial instruments recognised and measured at fair value

As at 31 December 2015	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Liabilities				
Derivative financial instruments	<u>(9,274,903)</u>	<u>-</u>	<u>(9,274,903)</u>	<u>-</u>

Financial instruments at amortised cost whose fair value is disclosed

As at 31 December 2015	Total fair value £	Level 1 £	Level 2 £	Level 3 £
Assets				
Mortgage loans	<u>150,872,577</u>	<u>-</u>	<u>150,872,577</u>	<u>-</u>
Liabilities				
Loan notes	<u>(140,007,150)</u>	<u>-</u>	<u>(140,007,150)</u>	<u>-</u>

During the year ended 31 December 2016, there have been no transfers between fair value hierarchy levels (2015: no transfers). In addition, there were no financial instruments that have been classified as level 3 and hence there is no need to disclose reconciliation of assets and liabilities categorised as level 3 instruments.

Interest rate risk

Interest rate risk exists where assets and liabilities have interest rates under a different basis or which reset at a different time. The Company minimises its exposure to interest rate risk by ensuring that the interest rate characteristics of assets and liabilities are similar. Interest rate swaps have been entered into with Deutsche Bank AG, London Branch to manage the Company's exposure to the interest rate risk associated with the mortgage loans. The swaps reduce interest rate risk as a result of the variance between the fixed rate of interest receivable on the mortgage loans and the variable rate of interest payable on the loan notes. As a result, the Company does not have a material net interest rate risk exposure and therefore has not presented a sensitivity analysis to interest rate risk.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Effective interest rates and repricing analysis

The following table details the Company's exposure to interest rate risk by the earlier of contractual maturities or re-pricing:

	Weighted average effective interest rate %	Floating £	Non-interest bearing £	Fixed rate £	Total £
At 31 December 2016					
Assets					
Trade and other receivables	-	-	1,419,282	-	1,419,282
Mortgage loans	4.654%	22,753,001	-	108,902,614	131,655,615
Cash and cash equivalents	-	56,984	-	-	56,984
Total assets		22,809,985	1,419,282	108,902,614	133,131,881

	Weighted average effective interest rate %	Floating £	Non-interest bearing £	Fixed rate £	Total £
Liabilities					
Trade and other payables and tax liabilities	-	-	1,988,485	-	1,988,485
Derivative financial instruments	-	657,761	-	-	657,761
Loan notes	0.825%	270,309,694	-	-	270,309,694
Total liabilities		270,967,455	1,988,485	-	272,955,940

	Weighted average effective interest rate %	Floating £	Non-interest bearing £	Fixed rate £	Total £
At 31 December 2015					
Assets					
Trade and other receivables	-	-	3,021,820	-	3,021,820
Mortgage loans	4.684%	27,036,272	-	139,171,974	166,208,246
Cash and cash equivalents	-	55,319	-	-	55,319
Total assets		27,091,591	3,021,820	139,171,974	169,285,385
Liabilities					
Trade and other payables and tax liabilities	-	-	2,584,983	-	2,584,983
Derivative financial instruments	-	9,274,903	-	-	9,274,903
Loan notes	1.000%	270,446,381	-	-	270,446,381
Total liabilities		279,721,284	2,584,983	-	282,306,267

Prepayment risk

Prepayment risk on the mortgage loans arises when these are voluntarily prepaid by the relevant borrower or borrowers thereof. With respect to all of the loans, such prepayment is contingent upon the payment of a prepayment fee. Any prepayment fees required to be paid by a borrower will be paid to Deutsche Bank AG, London Branch as part of the deferred consideration.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Capital risk management

The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern. The Company is not subject to any external capital requirements. The gearing ratios at 31 December 2016 and 2015 were 208% and 171.7% respectively.

Currency risk

All of the Company's assets and liabilities are denominated in Pound Sterling therefore there is no foreign currency risk.

Liquidity risk

Interest receipts on the mortgage loans may, under certain circumstances, be delayed. Such delays could adversely impact upon the ability of the Company to make timely payments of interest on the loan notes. In order to protect itself against this risk, the Company has entered into a liquidity facility agreement with Danske Bank A/S (London Branch) on 20 December 2006, as described in note 10.

Moreover, the maturity of the loan notes is designed to match the maturity of the mortgage loans and hence, there are deemed to be limited liquidity risks facing the Company.

The redemption of the notes is dependent on the receipt of payments on the mortgage loans. In accordance with the respective Prospectus for each of the loan notes, Class A-1A Notes will be redeemed in priority to redemption of the remaining classes of notes followed by Class A-1B, A-2, B, C, D, E and Class F. Interest payable on loan notes was estimated based on the floating rates as at 31 December 2016.

The undiscounted contractual cash flows for principal and interest on the loan notes have been disclosed in note 10.

The table below reflects the undiscounted contractual cash flows of non derivative financial liabilities at the reporting date.

As at 31 December 2016	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
Loan notes	270,309,694	270,309,694	27,000	261,936,431	8,346,263
Interest payable on loan notes	521,908	1,064,929	508,709	556,220	-
Total non-derivative financial instruments	270,831,602	271,374,623	535,709	262,492,651	8,346,263

As at 31 December 2015	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
Loan notes	270,446,381	270,446,381	30,000	45,709,061	224,707,320
Interest payable on loan notes	433,911	4,882,119	421,362	2,282,596	2,178,161
Total non-derivative financial instruments	270,880,292	275,328,500	451,362	47,991,657	226,885,481

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Liquidity risk (continued)

The above undiscounted contractual cash flows have been based on the assumptions that the repayment of the loan notes follows the same trend as the principal repayments on mortgage loans. The mortgage loans that are past due their legal maturity date have been assumed to be repayable in full within the next payment date.

The table below reflects the undiscounted contractual cash flows of derivative financial instruments at the Statement of Financial Position date.

As at 31 December 2016	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
	657,761	2,349,299	2,349,299	-	-
As at 31 December 2015	Carrying value	Gross cash flows	After 1 month but within 3 months	After 3 months but within 1 year	After 1 year but within 5 years
	£	£	£	£	£
	9,274,903	9,522,892	2,251,202	6,753,605	518,085

Credit risk

Credit risk on the mortgage loans arises where the mortgage loans are secured on underlying commercial properties. The maximum exposure to credit risk is the Statement of Financial Position amount. The largest single exposure to credit risk is the Mapeley Gamma mortgage loan totalling £108,902,614 net of provisions (2015: £139,171,974). This gives rise to a relatively high concentration risk of 83% (2015: 84%) as at year end. The Company monitors the performance of the loans on a regular basis and appoints third party specialist servicers, where required, to help maximise recoveries in the event of breaches or defaults on the loans. Solutus Advisors Ltd is the Special Servicer of the Mapeley Gamma properties.

The carrying amount of financial assets represents the maximum credit exposure.

The underlying mortgage loans are secured by first charge over commercial property located in England, Wales and Scotland.

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NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

12. FINANCIAL RISK MANAGEMENT (CONTINUED)

Credit risk (Continued)

The table below sets out the carrying amount, the collective impairments and approximate fair value of collateral held against exposures to customers. The estimate of fair value is based on the most recent valuation performed at different dates for each loan and are indexed at 31 December 2016 using the UK IPD property index, except for impaired loans where the directors' estimate of the collateral value was lower than the indexed valuation.

	Gross carrying amount 2016 £	Impairment 2016 £	Fair value of collateral 2016 £	Gross carrying amount 2015 £	Impairment 2015 £	Fair value of collateral 2015 £
Neither past due nor impaired	-	-	-	-	-	-
Past due but not impaired	-	-	-	-	-	-
Impaired	<u>261,963,432</u>	<u>(130,307,818)</u>	<u>131,655,614</u>	<u>262,100,120</u>	<u>(95,891,874)</u>	<u>166,688,396</u>
	<u>261,963,432</u>	<u>(130,307,818)</u>	<u>131,655,614</u>	<u>262,100,120</u>	<u>(95,891,874)</u>	<u>166,688,396</u>

The allowance for impairment disclosed above excludes impairment relating to written-off mortgage loans.

With regards to credit risk on derivatives, the directors monitor the credit rating of the swap counterparty and, in the case of any downgrade, may require the swap provider to provide sufficient collateral or transfer its obligations to another bank of the same credit rating.

13. DERIVATIVE FINANCIAL INSTRUMENTS

The net fair values of derivative financial instruments at the Statement of Financial Position date were:

	2016 £	2015 £
Interest rate swaps fair value at start of year	(9,274,903)	(18,692,334)
Change in fair value	<u>8,617,142</u>	<u>9,417,431</u>
Interest rate swaps fair value at end of year	<u>(657,761)</u>	<u>(9,274,903)</u>

The notional principal amount of all the outstanding interest rate swap contracts at 31 December 2016 was £216,361,059 (2015: £216,361,059). The Company pays a fixed rate ranging from 4% to 4.365% (2015: from 4.36% to 5.8%) and receives 3-month LIBOR (2015: 3-month LIBOR).

In accordance with IAS 39 'Financial instruments: Recognition and measurement', the Company has reviewed all contracts for embedded derivatives that are required to be separately accounted for if they do not meet certain requirements set out in the standard.

The Company has the ability to redeem the loan notes in full or part at their then principal amount outstanding, together with interest accrued to the date of redemption, on any interest payment date. The Company effectively has a call option on the loan notes exercisable on certain dates. The option constitutes an embedded derivative; however, as this is closely related to the underlying host contract (the loan notes) consistent with IAS 39, the option does not require separation. A similar hybrid instrument arises on the mortgage loan whereby the Company has effectively sold a put option on the mortgage loans exercisable on certain dates. As this option is considered to be closely related to the underlying host contract, it does not require separation.

DECO 11 – UK CONDUIT 3 PLC

NOTES TO THE FINANCIAL STATEMENTS (CONTINUED)

FOR THE YEAR ENDED 31 DECEMBER 2016

14. RELATED PARTY TRANSACTIONS

The Company is a special-purpose vehicle controlled by its Board of directors. Mr Graham Cox and Mr Graham Hodgkin are directors of the Company. Directors' emoluments during the year amounted to £4,800 (2015: £4,800) for their services as directors to the Company during the year. The Company paid corporate service fee to Deutsche Bank AG, London Branch, in connection with corporate services received. The fees payable to them for their services for the year ended 31 December 2016 amounted to £15,400 (2015: £15,400) including irrecoverable VAT with £nil (2015: £nil) still unpaid at year end.

15. ULTIMATE PARENT UNDERTAKING

Deco 11 – UK conduit 3 plc is a company incorporated in the United Kingdom and registered in England and Wales.

Deco 11 UK Conduit 3 Holdings Limited holds 49,999 shares in the Company. Castlewood CS Holdings holds one share in Deco 11 – UK Conduit 3 plc under a declaration of trust for charitable purposes. However, as a result of the terms of the notes issued by the Company, Deco 11 UK Conduit 3 Holdings Limited is not deemed to control the Company. Further neither the shareholders nor the directors have variable return over the Company and accordingly the Company has no Controlling party.

16. SUBSEQUENT EVENTS

There are no material post balance sheet events up to the date of approval of these financial statements.