Arrow Mortgage Finance No.1 Limited

Report and Financial Statements

Registration number 09891174

Year ended 31 December 2017

Contents

Strategic report

Introduction

The directors of Arrow Mortgage Finance No.1 Limited (the "Company") present their strategic report for the year ended 31 December 2017.

Business review

The Company forms part of a structure that has been established primarily as a means of raising finance for Nottingham Building Society.

The Company is a special purpose vehicle whose main activity is to act as a funding vehicle through which it has purchased the beneficial interest in certain residential mortgage loans in England and Wales (the "Loans" or "Mortgage Loans") from Nottingham Building Society (the "Originator"). The purchase was financed from the proceeds of a senior loan (the "Senior Loan") received by the Company. The Company's interest in the Mortgage Loans is represented by a deemed loan to Nottingham Building Society, as described in note 9.

In November 2017, the Company's interest in the Loans increased by £98 million to support an increase in the senior loan facility to £150 million. As a result of this amendment to the facility, the maturity date moved from January 2018 to May 2020.

During the year, Nottingham Building Society made repayments totalling £43,100,000 (2016: £9,823,000) to the Company in respect of the deemed loan. These repayments were used to repay part of the Senior Loan to the senior lender.

The key performance indicators used by management are consideration of whether there have been any breaches of the transaction documents, specifically:

- Expected available revenue income is sufficient to meet interest payable in respect of the Senior Loan; and
- All counterparties invoiced in the transaction have a rating that remains adequate to support their ongoing roles in the programme.

The Company has met these requirements throughout the current period.

The Company's key performance indicators for the Loans have been disclosed in note 16.

The key performance indicators used by management in assessing the performance of the Company are the excess spread within the transaction and the prepayment rate.

	2017	2016
Excess spread	0.73%	1.29%
Prepayment rate	3.2%	1.5%

Principal risks and uncertainties

The Company's objective for managing the principal risks and uncertainties it faces is to eliminate them as far as possible. Instruments used for risk management purposes are set up at inception of the transaction and include derivative financial instruments, such as an interest rate swap. This reflects the overall low risk appetite of the Company. After inception, no significant decisions regarding the risk management of the Company are required, but the interest rate position is monitored.

The financial risks faced by the Company are credit risk, liquidity risk and interest rate risk. A summary of these risks is listed below and more information regarding the management of these risks is included in note 16 of the financial statements.

Strategic report *(continued)*

Principal risks and uncertainties *(continued)*

Credit risk
Credit risk reflects the risk that the borrowers or other transaction parties may not meet their obligations as they fall due.

Credit risk on the Company's deemed loan asset is linked to the performance of the underlying mortgage assets and is considered to be minimal because the directors do not expect the amount of incurred credit losses of the Originators' Loans to exceed the amount of excess spread on the assets. A subordinated loan (the "Subordinated Loan") is also in place between the Company and Nottingham Building Society to further mitigate credit risk.

Credit risk from other transaction parties is managed through rating downgrade triggers that are written into the transaction documents.

Liquidity risk
Liquidity risk is the risk that the Company is not able to meet its financial obligations as they fall due, or can only do so at excessive cost. Liquidity risk arises on the Company's Senior Loan facility. However the payment schedule is linked to the principal received on the deemed loan assets and therefore liquidity risk is minimised. To protect counterparties should a shortfall arise, a reserve fund is held within the Company, which can be drawn upon to meet senior interest payments.

Interest rate risk
Interest rate risk arises from the interest rate mismatch between mixed rates on the Loans and the floating interest rate payable on the Senior Loan facility. The Company has fully hedged this risk using derivatives.

Operational risk
In order to meet its obligations to the Senior Loan provider, the Company has entered into contracts with third parties who have agreed to provide operational support to the Company in accordance with the facility agreement.

Intertrust Management Limited has been appointed to provide corporate services in accordance with a corporate service agreement. Other third parties who have agreed to provide services include the transaction account provider and swap provider. Nottingham Building Society acts as administrator and cash manager.

Future Developments

The directors consider that the Company will continue to meet the scheduled repayment dates for the Senior Loan in the foreseeable future using the cash generated from the mortgage assets.

Due to repayments decreasing the capital value of the mortgages, both the balance sheet and interest income will continue to decrease in future periods. The rate of decrease is dependent upon future redemptions.

This report was approved by the board and signed on its behalf:

Helena Whitaker
per pro Intertrust Directors 1 Limited
Director

20 March 2018

Directors' report

The directors present their report and the financial statements for the year ended 31 December 2017.

Results and dividends

The loss for the year, after taxation, amounted to £61,000 (period from 26 November 2015 to 31 December 2016: £207,000).

The directors do not recommend the payment of a dividend.

Directors

The directors who served during the year and up to the date of signing the financial statements were:

Claudia Wallace
Intertrust Directors 1 Limited
Intertrust Directors 2 Limited

None of the directors have any beneficial interest in the ordinary share capital of the Company.

Qualifying third party indemnity provisions for the benefit of the directors were in force during the period under review and remains in force as at the date of approval of the directors' report and financial statements.

Company secretary

Intertrust Corporate Services Limited have been appointed as company secretary and have served up to the date of signing the financial statements

Going concern

The Company is currently in a net liabilities position due to the current fair value position of derivatives held. However, due to the way in which the Company's activities are structured, the Company is only required to repay the Senior Loan facility in line with the controlled amortisation schedule on each payment date. Repayment is dependent on there being sufficient available principal receipts from principal repayments on the underlying Mortgage Loans. Consequently, the Directors are satisfied that the Company will have sufficient liquid resources available to meet its obligations as they fall due.

After reviewing the latest performance of the underlying mortgages, the Directors are satisfied that the Company will have adequate resources to continue in business for the foreseeable future and that it is appropriate to adopt the going concern basis in preparing the financial statements.

Disclosure of information to auditors

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

- so far as that director is aware, there is no relevant audit information of which the Company's auditors are unaware: and
- that director has taken all the steps that ought to have been taken as a director in order to be aware of any relevant audit information and to establish that the Company's auditors are aware of that information.

Directors' report *(continued)*

Auditors

The auditors, Ernst & Young LLP have expressed their willingness to continue in office and pursuant to Section 485 of the Companies Act 2006, a written resolution by the shareholder will be passed for the auditors' re-appointment.

This report was approved by the board and signed on its behalf:

Helena Whitaker
per pro Intertrust Directors 1 Limited
Director

20 March 2018

Directors' responsibilities statement

The directors are responsible for preparing 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, the directors have elected to prepare the financial statements in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law. Under Company law the directors must not approve the financial statements unless satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies in accordance with International Accounting Standard 8: Accounting Policies, Changes in Accounting Estimates and Errors and apply them consistently;
- present information, including accounting policies, in a manner that provides relevant, reliable, comparable and understandable information;
- state whether they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

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.

Independent auditor's report to the members of Arrow Mortgage Finance No.1 Limited

We have audited the financial statements of Arrow Mortgage Financial No.1 Limited for the year ended 31 December 2017 which comprise the Statement of comprehensive income, the Statement of financial position, the Statement of changes in equity, Cash flow statement and the related notes 1 to 19, including a summary of significant accounting policies. 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.

In our opinion, the financial statements:

- give a true and fair view of the company's affairs as at 31 December 2017 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.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report below. We are independent of the company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Use of our report

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

Conclusions relating to going concern

We have nothing to report in respect of the following matters in relation to which the ISAs (UK) require us to report to you where:

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

Other information

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

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

We have nothing to report in this regard.

Independent auditor's report to the members of Arrow Mortgage Finance No.1 Limited

Opinions on other matters prescribed by the Companies Act 2006

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

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

Matters on which we are required to report by exception

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 material misstatements in the Strategic report or directors' report.

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

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

Responsibilities of directors

As explained more fully in the directors' responsibilities statement set out on page 5, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view, and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

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

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

Ernst & Young LLP

Steven Robb (Senior statutory auditor)
for and on behalf of Ernst & Young LLP,
Statutory Auditor
Leeds

20 March 2018

Statement of comprehensive income
for the year ended 31 December 2017

	Notes	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
Interest receivable and similar income	3	**1,684**	968
Interest payable and similar charges	4	**(1,771)**	(890)
Net interest (cost)/ income		**(87)**	78
Movement in the fair value of derivatives	5	**151**	(210)
Administrative expenses	6	**(125)**	(75)
Loss before taxation		**(61)**	(207)
Tax expense	7	**-**	-
Loss for the period attributable to equity holders		**(61)**	(207)
Total comprehensive expense for the period		**(61)**	(207)

There were no recognised gains and losses for the financial year other than those included in the loss for the financial year above.

The loss for the year arises from continuing operations.

The notes on pages 12 to 23 form part of these financial statements.

Statement of financial position
as at 31 December 2017

	Notes	2017 £'000	2016 £'000
Assets			
Cash and cash equivalents	8	**7,880**	5,010
Deemed loans to Originator	9	**158,476**	101,591
Other assets	11	**2**	6
Total assets		**166,358**	106,607
Liabilities			
Interest bearing loans and borrowings	12	**20,079**	13,856
Derivative financial instruments	10	**78**	216
Loans from banks	13	**146,440**	92,717
Other liabilities	14	**29**	25
Total liabilities		**166,626**	106,814
Equity			
Share capital	15	**-**	-
Retained earnings		**(268)**	(207)
Total equity		**(268)**	(207)
Total equity and liabilities		**166,358**	106,607

The notes on pages 12 to 23 form part of these financial statements.

The financial statements were approved and authorised for issue by the board and were signed on its behalf by:

Helena Whitaker
Per pro Intertrust Directors 1 Limited
Director

20 March 2018

Registered number: 09891174

Statement of changes in equity
for the year ended 31 December 2017

	Share capital £'000	Retained earnings £'000	Total equity £'000
At 1 January 2017	-	(207)	(207)
Comprehensive income for the period			
Loss for the period	-	(61)	(61)
Other comprehensive income for the period	-	-	-
Total comprehensive income for the period	**-**	**(61)**	**(61)**
As at 31 December 2017	**-**	**(268)**	**(268)**

	Share capital £'000	Retained earnings £'000	Total equity £'000
At 26 November 2015	-	-	-
Issue of ordinary share capital	-	-	-
Comprehensive income for the period			
Loss for the period	-	(207)	(207)
Other comprehensive income for the period	-	-	-
Total comprehensive income for the period	-	(207)	(207)
As at 31 December 2016	-	(207)	(207)

The notes on pages 12 to 23 form part of these financial statements.

Cash flow statement
for the year ended 31 December 2017

	Notes	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
Cash flows from operating activities			
Loss before taxation		**(61)**	(207)
Increase in deemed loans to Originator	9	**(56,885)**	(101,591)
Decrease/(increase) in other assets	11	**4**	(6)
Increase in loans from banks	13	**53,723**	92,717
(Decrease)/Increase in derivative financial instruments	10	**(138)**	216
Increase in other liabilities	14	**4**	25
Net cash from operating activities		**(3,353)**	(8,846)
Cash flows from financing activities			
Increase in interest bearing loans and borrowings	12	**6,223**	13,856
Issue of share capital	15	**-**	-
Net cash from financing activities		**6,223**	13,856
Increase in cash and cash equivalents		**2,870**	5,010
Cash and cash equivalents at start of period		5,010	-
Cash and cash equivalents at end of period	8	**7,880**	5,010

The notes on pages 12 to 23 form part of these financial statements.

Notes to the financial statements

1. Accounting policies

a) *Basis of preparation*

These financial statements have been prepared in accordance with IFRSs as adopted by the European Union and applied in accordance with the Companies Act 2006. The financial statements are prepared under the historical cost convention as modified by the fair value of derivative financial instruments.

Changes to accounting policy

There were no new or amended standards or interpretations that have had a significant impact on the preparation of these financial statements.

Future accounting developments

A number of International Accounting Standards Board (IASB) pronouncements have been issued but are not effective for this financial period. The standards considered most relevant to the Company are as follows:

IFRS 9 'Financial Instruments' – effective from 1 January 2018. The standard will eventually replace IAS 39 and considers the impairment of financial assets, which will be based on expected credit losses rather than incurred losses as at present. The Company has assessed the impact that IFRS 9 will have on its financial statements, and it is not expected to have a material impact in respect of the impairment requirements of IFRS 9. There are no changes in the classification of financial assets and as the Company does not apply hedge accounting, this module is not applicable.

The following principal accounting policies have been applied consistently throughout the period.

b) *Segmental reporting*

The Company operates in one business segment and all business is conducted in the United Kingdom, therefore no segmental information is presented.

c) *Interest receivable and payable*

Interest receivable and payable is recognised in the Statement of comprehensive income for all instruments measured at amortised cost using the effective interest method.

The effective interest rate method calculates the amortised cost of a financial asset or financial liability and allocates the interest receivable or interest payable over the relevant period. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument, or when appropriate, a shorter period, to the net carrying amount of the financial asset or financial liability. When calculating the effective interest rate, the Company estimates cash flows considering all contractual terms of the financial instrument but does not consider future credit losses. The calculation includes all amounts received or paid by the Company that are an integral part of the overall return, direct incremental transaction costs related to the acquisition or issue of a financial instrument and all other premiums and discounts.

Interest receivable or payable on derivatives, whether in economic or accounting hedges is recorded on an accrual basis in interest receivable or payable.

d) *Taxation*

Tax on the profit or loss for the period comprises current tax. Tax is recognised in the income statement. Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted on the statement of financial position date and any adjustment to tax payable in respect of previous periods.

Notes to the financial statements *(continued)*

1. Accounting policies *(continued)*

e) *Financial assets*

Deemed loans to Originator
In accordance with International Accounting Standard 39 *Financial Instruments Recognition and Measurement* ("IAS 39"), where a legal transfer of a financial asset does not qualify for de-recognition in the financial statements of the transferor, the transferee does not recognise the transferred asset as its asset.

Nottingham Building Society, as the Originator, has retained substantially all the risks and rewards of ownership of the Mortgage Loans. De-recognition is considered to be inappropriate for the Originators' own financial statements, and therefore the Mortgage Loans remains on the statement of financial position of the Originator. The Company's financial statements are prepared on the basis that those acquisitions of beneficial interests in a Mortgage Loan are recognised as a collateralised loan to the Originator. The deemed loans to Originator are recorded at an amortised cost value equivalent to the cash consideration paid for the initial beneficial interest in the mortgage portfolio of the Originator at the time of transfer less any subsequent transfers and repayments of capital less deferred purchase consideration due.

Deferred consideration
Under the terms of the mortgage sale agreement, the Originators retain the right to receive surplus income generated by the underlying Mortgage Loans, where it exceeds the administration costs of the Mortgage Loan, credit losses and the interest payable on the Senior Loan facility. Since the Company does not recognise income to which it is not beneficially entitled to, deferred consideration payable is deducted from "Interest receivable and similar income" in the income statement. Similarly deferred consideration payable is also deducted from deemed loans to Originator in the statement of financial position.

Impairment of financial assets
The Company assesses its financial assets for objective evidence of impairment at each balance sheet date. An impairment loss is recognised if, and only if, there is a loss event that has occurred after initial recognition and on or before the balance sheet date, that has a reliably measurable impact on the estimated future cash flows of the financial assets. Losses that are incurred as a result of events occurring after the balance sheet date are not recognised in these financial statements.

f) *Financial liabilities*

Financial liabilities are contractual obligations to deliver cash or some other asset to a third party. They include the Senior Loan facility, interest bearing loans and borrowings and other liabilities.

Financial liabilities are recognised initially at fair value. Fair value includes the issue proceeds (the fair value of consideration received) net of issue costs incurred. Financial liabilities are subsequently stated at amortised cost. Any difference between issue proceeds net of issue costs and the redemption value is recognised in the income statement over the period of the borrowings.

Loans from banks represent a Senior Loan, classified as a liability as the contractual arrangements result in the Company having an obligation to deliver either cash or another financial asset to the security holder.

Interest bearing loans and borrowings comprise a Subordinated Loan provided by Nottingham Building Society. The loan will be repaid out of excess spread in accordance with the Company's priority of payments.

Notes to the financial statements *(continued)*

1. Accounting policies *(continued)*

g) Derivative financial instruments

The Company uses derivative financial instruments to manage its exposure to interest rate risk arising from investment activities. The Company does not hold or issue derivative financial instruments for trading purposes.

Interest rate risk associated with the deemed loan to Originator is managed by means of an interest rate swap, which requires the Company to pay the fixed rate relating to the beneficial interest in the mortgage portfolio and receive payments based on a rate linked to the one month LIBOR.

IAS 39 requires all derivative financial instruments to be recognised initially at fair value on the balance sheet. Subsequent to initial recognition, derivatives are re-measured 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 re-measurement to fair value is recognised immediately in the statement of comprehensive income. The fair value of interest rate swaps are the estimated amount that the Company would receive or pay to terminate the swap at the balance sheet date.

h) Cash and cash equivalents

The Company holds deposits and a bank account. These accounts are held in the Company's name and meet the definition of cash and cash equivalents.

For the purpose of the cash flow statement, cash and cash equivalents comprise liquid asset balances with less than three months maturity from the date of acquisition.

i) Loans from banks

The terms and conditions of the senior facility state that the date of termination of the facility is in May 2020. The effective interest rate has been calculated based on the assumption that the facility will be fully repaid at the termination date. In November 2017, the Company's interest in the portfolio of mortgage assets increased by £98 million to support an increase in the Senior Loan facility to £150 million. As a result of this amendment to the facility, the maturity date moved from January 2018 to May 2020.

2. Significant accounting judgements and estimates

The preparation of the financial statements in conforming to the use of IFRS as adopted by the EU requires the use of certain critical judgements and estimates. The areas involving judgements and estimates are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the current or normal operating circumstances.

In the process of applying the Company's accounting policies, the directors have made the following judgements and estimates that have the most significant effect on the amounts recognised in the financial statements.

Loans and other debts due from Originator – recognition
As the Originator has retained substantially all the risks and rewards of ownership of the mortgage portfolio, de-recognition is considered to be inappropriate for the Originators' own financial statements, and therefore, the Mortgage Loans remain on the statement of financial position of the Originator. Consequently, the Company recognises a deemed loan to the Originator, rather than the underlying mortgage assets.

Notes to the financial statements *(continued)*

2. Significant accounting judgements and estimates *(continued)*

Judgement is required in assessing whether risks or rewards of ownership of the mortgage portfolio have transferred. The factors considered in arriving at the conclusion that risk and rewards were not transferred include, that the Originator continues to retain the right to receive excess income arising on the Mortgage Loans (excess profit), after certain priority payments have been made by the Company. Furthermore the Originator and the Company entered into a derivative transaction which pays substantially all the mortgage interest to the Originator and pays a floating rate to the Company. In addition, under the terms of the facility, the Originator also acquired a holding in a Subordinated Loan, which are considered the first items linked to losses suffered on the mortgage portfolio.

Recoverability of deemed loan to Originator
The recoverability of the deemed loan to Originator is dependent on the collections from the secured mortgages, as the term of the deemed loan links the repayment of the deemed loan to the repayment received on these mortgages.

The secured mortgages are considered impaired when it is probable that the Originator will be unable to collect all amounts due according to the contractual terms of the agreement. The key assumptions for recoverability relate to estimates of the probability of an account going into default and the timing and amount of any cash flows received from the borrowers. Delinquencies and defaults on the secured mortgages will not result in any impairment as long as they do not exceed the excess spread that is available to make good any reductions in the principal balance of the mortgages as a result of defaults by customers.

At each statement of financial position date, the Company assesses whether there is any objective evidence that the deemed loan to Originator is impaired, and have concluded that there is no such evidence.

3. Interest receivable and similar income

	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
On deemed loans to Originator	**2,647**	1,479
Excess profit payable	**(963)**	(511)
	1,684	968

Notes to the financial statements *(continued)*

4. Interest payable and similar charges

	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
On loans and borrowings	181	85
On loans from banks	1,138	642
Amortisation of issue costs	272	119
On derivative financial instruments	180	44
	1,771	890

5. Movement in the fair value of derivatives

	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
Derivatives not in designated fair value hedge relationships	(151)	210

The Company has entered into a derivative financial instrument, which although effective as an economic hedge, is not included in hedge accounting relationships. This derivative hedges the difference between the interest rate applicable to the Mortgage Loans in the portfolio and the floating rate of the interest on the Senior Loan facility.

6. Administrative expenses

	Year ended 31 December 2017 £'000	Period from 26 November 2015 to 31 December 2016 £'000
Cash manager fees	8	4
Mortgage servicer fees	78	40
Other administrative expenses	39	31
	125	75

The Company employed no employees during the period. Nottingham Building Society acts as the Servicer of the mortgage portfolio and the Cash Manager under the terms of the facility agreement.

None of the directors directly received any emoluments during the period for their services to the Company nor received any benefits from the Company. The directors are employed and remunerated by Intertrust Management Limited, who are the appointed corporate service provider and earned a fee of £17,000 (2016: £13,000) for the period in respect of their corporate administration services for the Company.

Audit fees for the period, excluding VAT, total £12,875 (2016: £12,500).

Notes to the financial statements *(continued)*

7. Taxation

The current tax charge for the period was £231 (2016: £118), but has been presented as £nil due to the financial statements being presented in £'000.

The charge has been calculated in accordance with the permanent regime for taxation of securitisation companies. This secondary tax legislation ensures that, for companies who satisfy certain conditions, including the definition of a warehousing or securitisation company, corporation tax will be calculated by reference to its retained profits not its accounting profit or loss.

The Finance Act 2015 reduced the future rate of UK corporation tax from 20% to 19% with effect from 1 April 2017. Furthermore, the Finance Act 2016, following its enactment in September 2016, reduced the future rate further to 17% with effect from 1 April 2020.

8. Cash and cash equivalents

	31 December 2017 £'000	31 December 2016 £'000
Cash and cash equivalents	**7,880**	5,010

9. Deemed loans to originator

The sale of the beneficial interest in the Mortgage Loans, even though legally acquired from the Originator, does not pass the de-recognition criteria as described in IAS 39 and therefore deemed loans to Originator are shown in the Company's Statement of financial position.

	31 December 2017 £'000	31 December 2016 £'000
Deemed loans	**158,505**	101,629
Deferred consideration payable	**(29)**	(38)
	158,476	101,591

The Mortgage Loans are all denominated in Sterling and are at a fixed rate of interest. The maturity of the deemed loans due from Nottingham Building Society is calculated on the basis of the contractual maturity profile of the underlying Mortgage Loans. The deemed loans to Originator are repaid as and when cash is received by the Originator from the customer as principal repayments of the secured mortgages.

Notes to the financial statements *(continued)*

10. Derivative financial instruments

The Company uses derivative instruments for the purpose of supporting the strategic and operational business activities and reducing the risk of loss arising from changes in interest rates. All use of derivative instruments is to reduce risk exposure.

	Contract/ notional amount £'000	Fair value of assets £'000	Fair value of liabilities £'000
Fair values at 31 December 2017			
Interest rate swaps	**155,878**	**-**	**(78)**
Fair values at 31 December 2016			
Interest rate swaps	106,378	-	(216)

The fair value above includes accrued interest payable of £19,000 (2016: £5,000).

11. Other assets

	31 December 2017 £'000	31 December 2016 £'000
Other receivables	**2**	6

12. Interest bearing loans and borrowings

	31 December 2017 £'000	31 December 2016 £'000
Subordinated loan from Nottingham Building Society	**20,079**	13,856

Interest bearing loans and borrowings comprise a Subordinated Loan from the Seller. Interest and principal is repaid on the loan in accordance with the priority of payments specified dependent on available revenue and principal receipts. The Subordinated Loan bears interest at a rate equivalent to 1 month LIBOR plus a margin. The Subordinated Loan increased in November 2017 as a result of the top up of the senior facility agreement.

Notes to the financial statements *(continued)*

13. Loans from banks

	31 December 2017 £'000	31 December 2016 £'000
Senior loan	**146,534**	92,984
Less unamortised issue costs	**(94)**	(267)
	146,440	92,717

The Senior Loan is contractually repayable in May 2020, but will pay down on each monthly payment date to the extent that principal repayments have been received in respect of the Company's deemed loan due from Nottingham Building Society. Interest is payable at a margin over 1 month LIBOR. The Company has not had any defaults of principal, interest or other breaches in respect of the Senior Loan during the year. In November 2017, the Company's interest in the portfolio of Mortgage Loans increased by £98 million to support an increase in the Senior Loan facility to £150 million. As a result of this amendment to the facility, the maturity date moved from January 2018 to May 2020.

14. Other liabilities

	31 December 2017 £'000	31 December 2016 £'000
Amounts owed to group undertakings	**12**	8
Accruals	**17**	17
	29	25

15. Share capital

	31 December 2017 £'000	31 December 2016 £'000
Called up and allotted		
1 ordinary share of £1 issued and fully paid up	**-**	-

16. Financial instruments

The Company has not had any defaults on principal, interest or any other breaches with respect to their liabilities during the period.

The narrative disclosures required by IFRS 7 in relation to the nature of the financial instruments used during the period to mitigate credit, interest rate and liquidity risk are presented in the Strategic report on page 1.

The Company's exposure to risk on its financial instruments and the management of such risk is largely determined from inception of the transaction. The Company's activities and the role of each party to the transaction is clearly defined and documented within the transaction documents. Nottingham Building Society manages the Mortgage Loans under the terms of its servicing agreement with the Company. In managing the Mortgage Loans, Nottingham Building Society applies its formal structure for managing risk and other control procedures.

Notes to the financial statements *(continued)*

16. Financial instruments *(continued)*

Summary

The table below summarises the main financial instruments, their significant terms and conditions and the accounting treatment adopted.

Financial instrument	Terms and conditions	Accounting policy
Deemed loans to Originator	Long term Fixed interest rate	Amortised cost
Cash and cash equivalents	Short term cash balances	Amortised cost
Loans and advances to credit institutions	Short to medium term maturity	Amortised cost
Loans from banks	Long term Floating interest rate	Amortised cost
Interest bearing loans and borrowings	Long term Floating interest rate	Amortised cost

Classification and fair value measurement

Fair values of financial assets and liabilities carried at amortised cost

The following table analyses the carrying values and fair values of the Company's financial instruments held at amortised cost at 31 December.

	31 December 2017		31 December 2016	
	Total Book value £'000	**Total Fair value £'000**	Total Book value £'000	Total Fair value £'000
Financial assets				
Deemed loans to Originator	**158,476**	**159,073**	101,591	102,670
Financial liabilities				
Interest bearing loans and borrowings	**20,079**	**20,079**	13,856	13,856
Loans from banks	**146,440**	**146,440**	92,717	92,717

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 measurement date. The estimated fair value of the financial assets and liabilities above has been calculated using the following valuation methodology:

Level 1: Quoted prices (unadjusted) 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 or indirectly.
Level 3: Inputs for the asset or liability that are not based on observable market data.

Deemed loan to Originator – level 3: The estimated fair value represents the discounted amount of estimated future cash flows expected to be received taking into account of expected prepayment rates.

Interest bearing loans and borrowings – level 3: The estimated fair value represents the discounted *amount of estimated future cash flows expected to be received taking into account of expected* prepayment rates.

Loans from banks – level 3: The fair value is calculated using a discounted cash flow model. Expected cash flows are discounted at prevailing market rates for items of similar remaining maturity.

Notes to the financial statements *(continued)*

16. Financial instruments *(continued)*

Risk management

Credit risk

Credit risk is the risk that a customer or counterparty will not be able to meet its obligations to the Company as they become due. Credit risk arises on cash and cash equivalents and the deemed loans to Originator. The ability of the Originator's customers to repay their loans is impacted by the economic factors in the United Kingdom.

Maximum credit risk exposure at 31 December 2017 approximates to the carrying value for all assets and loan commitments, as presented below, without taking into account any collateral held. The table also shows the maximum exposure to credit risk on deemed loans. The risk on deemed loans is mitigated by the size and quantity of the underlying Mortgage Loans.

	31 December 2017 £'000	31 December 2016 £'000
Assets		
Deemed loans to Originator	**158,476**	101,591
Cash and cash equivalents	**7,880**	5,010
	166,356	106,601

Deemed loans to Originator

The table below presents the indexed loan to value percentage of the underlying mortgage portfolio to which the deemed loans to Originator relates to as at the end of the reporting period.

	31 December 2017		31 December 2016	
	Mortgage Balances £'000	**Number of accounts No**	Mortgage Balances £'000	Number of accounts No
Indexed loan to value on underlying mortgage portfolio				
<50%	**17,398**	**148**	2,854	28
50% - 65%	**64,190**	**441**	3,774	25
65% - 75%	**60,503**	**379**	18,811	132
75% - 85%	**16,521**	**94**	70,128	463
>85%	**124**	**1**	6,803	51
	158,736	**1,063**	102,370	699

Notes to the financial statements *(continued)*

16. Financial instruments *(continued)*

Risk management

Credit risk (continued)

The table below presents information by payment due status on the underlying mortgage portfolio to which the deemed loans to Originator relates to as at the end of the reporting period.

	31 December 2017 £'000	31 December 2017 %	31 December 2016 £'000	31 December 2016 %
Arrears analysis				
Not impaired:				
Neither past due or impaired	**158,558**	**99.9**	102,370	100.0
Past due up to 3 months but not impaired	**178**	**0.1**	-	-
Impaired				
Neither past due or impaired	-	-	-	-
	158,736	**100.0**	102,370	100.0

Credit risk in respect of cash and cash equivalents and other transaction parties is managed through rating downgrade triggers that are written into transaction documents. There has been no breach of any triggers in the period.

Liquidity risk

Liquidity risk is the risk that the Company has insufficient funds to meet its financial obligations as they fall due. The following is an analysis of gross contractual cash flows payable under financial liabilities.

Residual maturity	Repayable on demand £'000	Not more than 3 months £'000	More than 3 months but not more than 6 months £'000	More than 6 months but less than one year £'000	More than one year but not more than 5 years £'000	Total £'000
As at 31 December 2017						
Interest bearing loans & borrowings	-	-	-	-	20,079	20,079
Loans from banks	-	6,701	4,850	15,909	118,980	146,440
	-	**6,701**	**4,850**	**15,909**	**139,059**	**166,519**
As at 31 December 2016						
Interest bearing loans & borrowings	-	-	-	-	13,856	13,856
Loans from banks	-	10,136	13,423	18,020	51,138	92,717
	-	**10,136**	**13,423**	**18,020**	**64,994**	**106,573**

Due to the direct relationship between principal receipts of the underlying Mortgage Loans and the repayment of the Senior Loan facility, the Senior Loan is likely to be repaid earlier than the contractual maturity date of May 2020. Therefore for the purpose of this disclosure, the repayment of the principal receipts have been estimated over three years with any outstanding principal receipts being assume to be repayable during May 2020.

Notes to the financial statements *(continued)*

16. Financial instruments *(continued)*

Risk management

Liquidity risk (continued)

Prepayment risk arises when it is possible that the assets may be realised earlier than it is possible to redeem the liabilities. The risk is mitigated by the pass through attributes of structure whereby all principal payments on the underlying Mortgage Loans are used to redeem the Senior Loan facility.

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 fully hedging the difference between the interest rate characteristics of the mortgage portfolio and the Senior Loan facility.

The Company is exposed to interest rate risk in that its interest expense is LIBOR based, whilst its interest income originates from its beneficial interests in pools of mortgages at fixed rates. The Company hedges this interest rate exposure through entering into a derivative.

17. Ultimate parent undertaking and controlling party

The issued share capital of the Company is held entirely by Intertrust Corporate Services Limited on a discretionary trust basis for the benefit of certain charities. Copies of the financial statements of Intertrust Corporate Services Limited, a company incorporated in the United Kingdom and registered in England and Wales, may be obtained from 35 Great St Helen's, London, EC3A 6AP.

For accounting purposes, the Company's ultimate controlling entity is Nottingham Building Society. The Company's results are included within the consolidated financial statements of the Society, which are available from Nottingham House, 3 Fulforth Street, Nottingham, NG1 3DL.

18. Related party transactions

The Company is a special purpose vehicle, with all of the Company's directors provided by Intertrust Management Limited. The Company pays a corporate service fee to Intertrust Management Limited in connection with its supply of corporate management services, including the provision of directors. The total amount paid in the year, including other disbursements and VAT was £17,318 (2016: £19,000), which includes a prepayment of £1,000 (2016: £6,000) for fees earned for 2017 services.

Nottingham Building Society holds 100% of the Subordinated Loan (note 12). The interest payable on this loan in 2017 totalled £181,000 (2016: £85,000).

19. Registered office

Arrow Mortgage Finance No. 1 Limited is a company, incorporated and domiciled in the United Kingdom. The address of its registered office is: 35 Great St. Helen's, London, EC3A 6AP.