Ecology Building Society

Contents

Society Information

Directors	Malcolm Lynch	*Chair*
	Tony Taylor	*Deputy Chair*
	Helen Ashley Taylor	(appointed May 2012)
	David Black	
	Mark Jones	
	Steven Round	
	Paul Ellis	*Chief Executive*
	Pam Waring	*Secretary*
Registered office	7 Belton Road Silsden Keighley West Yorkshire BD20 0EE	
External auditors	KPMG Audit Plc St James Square Manchester M2 6DS	
Internal auditors	Deloitte LLP 1 City Square Leeds LS1 2AL	
Lawyers	Addleshaw Goddard Sovereign House Sovereign Street Leeds LS1 1HQ	
Officers	George Haslem	*Chief Operating Officer*
	John Ainley	*Compliance Manager*
	Anna Laycock	*Communications and Research Manager*
	Jon Lee	*Business Development Manager*
	Richard Saville	*Technology Manager*

Chair's Statement

In February, Barclays' new Chief Executive announced a strategic overhaul of the bank, in response to "a period of 20 years in banking in which the sector became too aggressive, too focused on the short term and too disconnected from the needs of customers and clients and wider society."

This may be a new realisation for Barclays, but it is certainly not for Ecology Building Society. I am pleased to report that your Society has continued its original policy of thinking long-term, providing products which are focussed on the needs of our members and which contribute to wider social and environmental benefit rather than being designed purely for profit. These are policies which the Board fully supports and which our Chief Executive and management team ensure are put into practice in the daily business of Ecology.

It is these polices that allow me to report that our assets have increased to almost £110 million, with higher growth than we originally forecast for the year. Our profits were far higher than forecast, for the reasons set out in the Chief Executive's Report. This profit has added to our capital base, increasing the financial strength of the Society and our ability to undertake further lending to new borrowers in the year ahead.

The Board made steady progress during the year with defining the type of capital instrument required before making a public offer. The European Rules on capital instruments have been delayed and it has been something of a guessing game to anticipate them. We have agreed that it is best to approach our search for capital in a careful and methodical fashion and there have been no pressures on the Society which would require a different course. We will continue to update those members who have expressed an interest in investing in our capital base as our work develops.

During 2012 we continued to develop our offering to meet the urgent need to improve the energy efficiency of the nation's 27 million homes. While the government's Green Deal proposals met with a mixed reception from the industry and struggled to achieve public awareness, we launched our pilot 'Fair Green Deal' with The Energy Saving Co-operative, offering maximum benefit for communities and access to ethical sources of finance. Along with our network of partners, our innovative work is paving the way for mainstream adoption of sustainable building practices.

Our forthcoming Annual General Meeting will see the planned retirement of David Black and Mark Jones as Directors of the Society. On behalf of the Board, I thank David for his forensic accounting questions which have probed the Society's finances so effectively, and to Mark for his diligent contributions as a smallholder borrowing member, keeping the Board in touch with the Society's roots.

I have also to report that Adam Clark resigned from the Board at the end of the year. He decided that balancing his commitment to his busy architect's practice with the high standard of understanding which he wished to have of the regulatory environment presented too great a challenge. Adam has expressed his willingness to continue to assist the Society with his specialist eco-architectural knowledge, for which we are most grateful. 2012 also saw the planned retirement of Janet Slade, who brought to the Board a unique combination of accountancy expertise and environmental focus. Janet continues to act as a Trustee and Treasurer of the Ecology Building Society Charitable Foundation. The Board was strengthened in May by the appointment of Helen Ashley Taylor, who is a qualified accountant with experience of the charity and mutual sectors and has already made a significant contribution to our work.

We enter 2013 with high hopes and a continued commitment to demonstrating that long-term, socially useful finance can be sustainable in every sense of the word. I wish to thank you for your continued support and engagement with the Society and I look forward to welcoming you to our 32nd Annual General meeting in April.

Malcolm Lynch
Chair

25 February 2013

Chief Executive's Review

Overview

In an eventful year, the Society experienced good growth, good profit, good net lending, and a good inflow of funds. Good because it was positive financial progress, but good fundamentally because all this was achieved by adherence to our core principles in the pursuit of sustainability. The Society is increasingly seen as a leader in this respect, both through its persistence and its role as an innovator.

The Society also benefitted from the attention given by external campaigns such as ***Move Your Money,*** which drew attention to the services provided by financial institutions with a social remit and the mutual sector. As the Society grows its lending portfolio, it will be able to absorb even more deposits from new members who have been alerted to our existence by these grass-roots campaigns. Because of the strong flow of funding, we do not anticipate accessing the Government's ***Funding for Lending Scheme***, which has further reduced rates to savers. As long-standing members know, our view of mutuality in any case requires us to maximise the extent to which we attract funding via ethical savings, in preference to taking money from the markets.

The ***C-Change*** mortgage discounts continued to pick up awards, and figure in a growing proportion of our mortgage book, which is enabling us to track the increased energy efficiency standards represented by the type of properties we lend on when compared against the general condition of the UK housing stock.

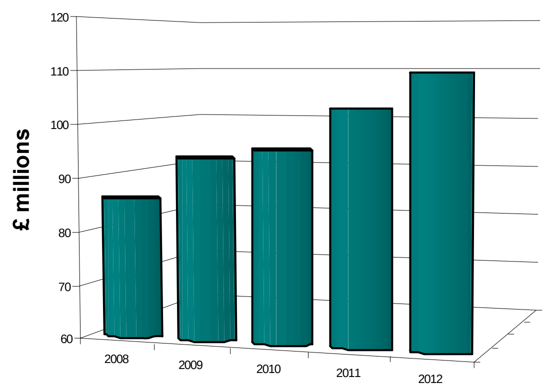
Indeed, during 2012 we undertook much work to improve the way we collect information on our social impact, the results of which will become increasingly apparent in future reports from the Society. The conceptual framework for this has been developed by Anna Laycock, who has now also taken on additional responsibilities as our first ***Ethics Manager***. Anna's role is to ensure that we continue to embed our ethos across what we do as a business, and thereby ensure good conduct in pursuit of our mission

After the extensive recruitment in 2011, our activity in 2012 year was more restrained as the new team got to work. However, we were pleased to welcome our first Graduate Trainee in **Charlotte Leggett**, who comes to us with a background in Ecological Economics. We are constantly looking to ensure that we have the right people to take the Society to the next level, with the appropriate skills, and we will again be adding to our team in the coming year.

So, as a Society we enter 2013 with a sense that much of the preparatory work we have undertaken in 2012 will begin to bear fruit in the coming year. More detailed commentary on the year is given below, including the key performance indicators that the Board uses to measure the Society's financial progress, the service we provide to our members, and our impact on the environment and community. Each of the sections below contains comment in ***green*** to indicate specific responses to environmental responsibility and good corporate governance.

Asset growth

Strong growth in assets was again achieved at 6.1% (2011: 8.1%). This was fuelled by the inflow of members' deposits and we experienced a positive inflow in every month of the year – the last monthly outflow encountered was in fact back in 2010. Nevertheless, we believe in restricting the level of uncommitted funds held, even at the expense of overall growth, as we do not feel it sits well with the mission of the Society to take in excessive funds we cannot immediately use for projects that meet our lending criteria. To do so would distort the market for ethical deposits and reduce the social and environmental dividend obtained by our members. We are able to absorb these strong flows of funds from members by continuing to expand our sustainable mortgage book, which is our priority for 2013.

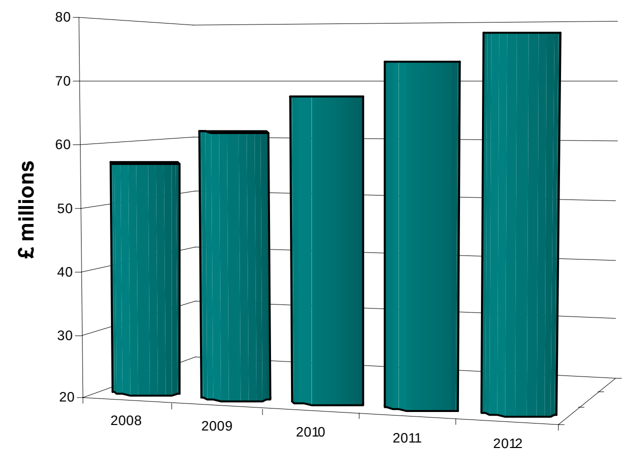


Total Assets

Chief Executive's Review *continued*

Mortgage lending

Overall mortgage asset growth dropped slightly in percentage terms from the previous year, amounting to 6.0% (2011: 7.6%), but overall mortgage balances exceeded £75m for the first time. In monetary terms, net lending remained strong at £7.9m, despite the effect of redemptions of non-performing cases. While the net lending performance is good as it supports the profitability of the Society and demonstrates our ability to retain mortgage customers, ***the focus of the Society's management remains on the gross lending figures as this represents new lending and therefore more properties undergoing ecological transformation. Consequently, it is a stronger indicator that the Society is fulfilling its primary purpose in promoting an environmentally informed lending programme. The increase in mortgage assets shows that the lending proposition of the Society continues to serve the needs of our borrowing community.***



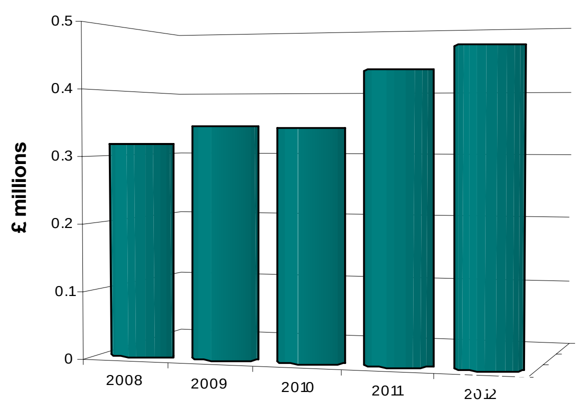
Mortgage Assets

Total provisions against possible mortgage losses have reduced significantly to £196,000 (2011: £659,000). This first of all reflects the fact that losses of £413,000 were incurred on the sale of a number of properties in possession. However, the losses were less than the sums provided and so some of the provisions have been written back to profit. Finally, as no new cases have emerged with a potential of loss, there has been no need to make new provisions. This indicates that overall the mortgage book is performing well and suggests that the worst effects of the financial crisis have now been weathered. Nevertheless, it is clear that the economy now operates at a lower level of output than before the financial crisis, so there is still potential for borrowers to encounter difficulties. ***We advise borrowers to seek free advice about problem debt from specialist counselling services. We will continue wherever possible to exercise forbearance, where the risk to the borrower is not unduly increased, to give the borrower breathing space to sort out their financial affairs, in the form of payment holidays, changes to payment schedules, interest-only arrangements and amendments to the term of the mortgage.***

Profit and capital

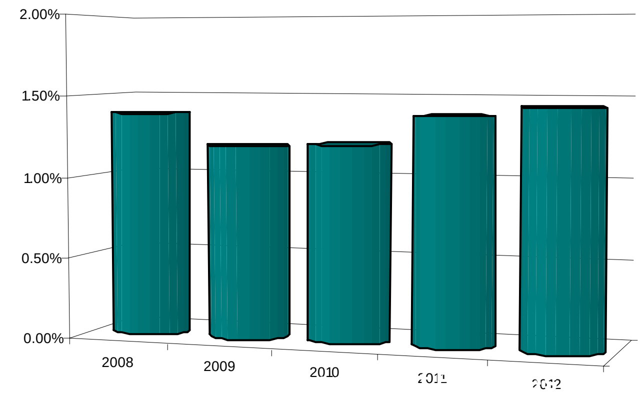
The Society aims to generate sufficient profit from its activities to ensure that it has enough capital to underpin its future lending programme and other business assets.

The Society again performed strongly in terms of profit and therefore the addition to capital resources. Net profit (surplus) for the year at £459,000 was 8% higher (2011: £425,000). Profit as a percentage of assets remained at the same level as in 2011. Members need to be aware that the profit levels are currently depressed by the ongoing need to contribute to the resolution arrangements for a number of failed financial institutions, including the Bradford and Bingley. The provision made in this respect for 2012 amounted to 11.6% of the overall gross profit of the Society. Net profit adds directly to the capital of the Society, and it is important to increase capital resources in line with increased demand for the services of the Society, thereby protecting members' funds from the effect of any future potential losses. Increased capital also increases our ability to lend in absolute terms and to consider lending on larger projects.



Profit

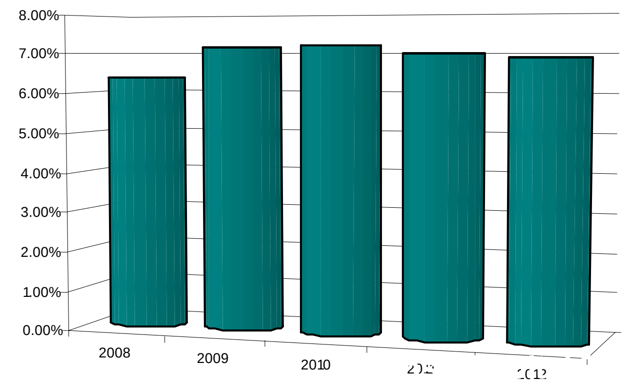
Chief Executive's Review *continued*



Management Expenses Ratio

The Management Expenses Ratio increased to 1.45% (2011: 1.39%), mainly because of increase in costs associated with compliance and legal advice regarding changes to our rules, which was not offset by overall growth in the Society's assets. Overall administration costs grew by 11.34% in comparison to 21.85% in 2011. ***Wherever possible we use the most sustainable and ethical option when purchasing goods and services. Sometimes this means that we have to pay a little more than the unsustainable option. We have tracked the additional costs where this has occurred during 2012 and found that our ethical purchasing policy increased our management expenses by 4.63%. If we had not factored environmental and ethical impacts into our procurement, our Management Expenses Ratio for 2012 would be 1.39%.***

The Gross Capital Ratio reduced slightly in 2012 to 6.98% (2011: 7.03%). This was due to the start of amortisation of a tranche of supplementary capital that the Society holds in the form of subordinated debt. The value of this type of debt in capital terms reduces in the last five years of the term it is held for. We intend to continue to seek supplementary capital in addition to retained profit, to enable continued growth of the Society.

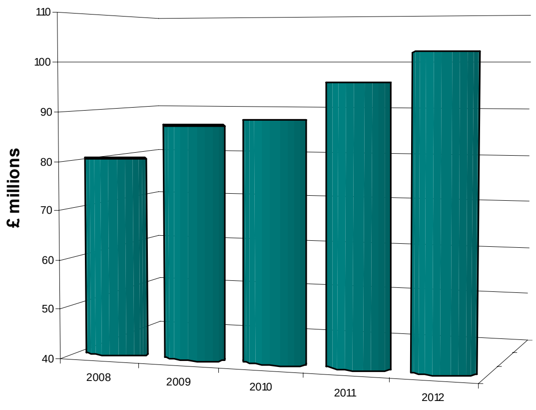


Gross Capital Ratio

Savings and Liquidity

Savings balances increased by 5.99% (2011: 8.45%), from £96.14m in 2011 to £101.90m by the end of 2012. ***Throughout the year, the Society continued its longstanding commitment to never pay less than 1.00% interest to savers.*** The Society experienced an inflow in every month of the year, and the task was to ensure that until lending volumes can be increased further, inflow of funds did not reach such levels that liquidity increased unsustainably.

In fact, liquidity levels were once again stable, increasing slightly to 30.16%, from 30.03% in 2011. Holding excess liquidity is a cost to the Society, especially when market rates are at record lows. In addition, ***we have always maintained that holding more liquidity than required for prudential reasons does not fit with the ethical savings model as it distorts interest rates in the market and means that a higher proportion of your deposit is not used to support social and environmental lending projects. It necessarily remained the case that in 2012 counterparties (banks and other building societies) were selected primarily for their financial safety rather than as a result of our established policy of examining their environmental and ethical practice record – which we continue to monitor and record.*** However, the outcome of this was ameliorated somewhat by the regulatory requirement that institutions hold a significant proportion of their liquidity in the form of UK Government treasury instruments.

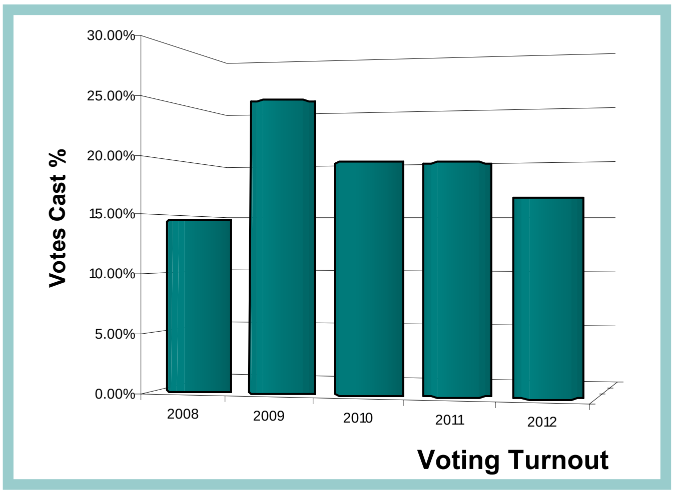


Savings Balances

Chief Executive's Review *continued*

Member relations

In 2012, we took our AGM to the north-east of England for the first time. The north-east is not traditionally our strongest region, but we wanted to continue our tradition of taking the AGM to the members. The AGM was held at the Rivergreen Centre in Durham, a green building featuring rammed earth walls. We always hold a Green Marketplace alongside the AGM, and we have developed a number of new opportunities for the Society in the north-east from the contacts made. The proportion of members voting electronically rose to 32.38% from 31.65% in 2011, while the actual number of members voting reduced to 16.32% from 19.17%. ***The theme of the day was the individual actions that we can all take to reduce our environmental impact – including renovation of our own properties of course!***



Our place in the community

Our commitment to change extends beyond the immediate impact of our mortgage lending. As a mutual, we look for the widest application of mutual governance in the economy and society, an expanded democratic space and by extension the support and growth of sustainable, cohesive communities with the potential to exercise control over their own wealth and wellbeing. This is the basis of our giving of both time and money.

The Society is a member of a number of organisations which share our wider values. Some are listed below:

The Sustainable Building Association (AECB)	A network of individuals and companies with a common aim of promoting sustainable building
Passivhaus Trust	An independent, non-profit organisation that promotes the adoption of the Passivhaus standard
Schumacher Society	Non-profit organisation promoting human-scale development
UK Sustainable Investment and Finance Association (UKSIF)	Membership network for sustainable and responsible financial services
Locality	The nationwide network for development trusts and community enterprises
Northern Ireland Environment Link	Northern Ireland's forum and networking body for organisations interested in the environment
Scottish Ecological Design Association (SEDA)	SEDA aims to promote design which enhances the quality of life of and does not harm planetary ecology
Woodland Trust	The UK's leading woodland conservation charity

During 2012 we also rejoined the Forum for the Future, a leading advocate of sustainability in business practice, having welcomed students from the Forum's Graduate programme for a number of years. In international terms we continued to be active participants in both the Institute of Social Banking and the International Association of Investors in the Social Economy (INAISE).

Over the course of the year we provided financial support to a wide variety of organisations and initiatives that contribute to sustainability at a local, national or international level, either directly through the Society or via our associated charitable foundation. These included:

- ***INAISE Conference, Paris – How can social finance help address the effects of climate change?***
- ***Leeds Empties Week – tackling empty homes in Leeds***

Chief Executive's Review *continued*

- ***Compton's Yard Charitable Trust, Llanidloes – a grant towards the cost of insulating a listed building used as a community hub***
- ***Whirlow Hall Farm Trust, Sheffield – an educational trust working with inner city children and young people with special needs and disabilities***
- ***Green Gathering, Chepstow – ethical and environmental family festival.***

We also gifted time to a number of organisations including the International Association of Investors in the Social Economy (INAISE), Passivhaus Trust, Leeds Community Foundation and the HALE Project (a health charity operating in West Yorkshire).

Our Earthsaver Bonds continued to generate donations for Practical Action, the leading international development charity. We maintain shareholdings in social ventures such as the Ethical Property Company and the Phone Co-op, and where possible we place funds with other social economy financial institutions such as Charity Bank.

The three main internal developments regarding our Environment Policy in 2012 were that:

- ***Directors and staff undertook further training on environmental awareness and carbon management***
- ***We improved our procurement procedures to better ensure positive social and environmental outcomes***
- ***A 10kWth (kilowatt thermal) solar water heating system was installed at the HQ building.***

Our main commitments for 2013 are to:

- ***Revisit our offsetting obligations and policy to ensure that we maintain absolute carbon neutrality***
- ***Re-configure and upgrade heating and ventilation systems, as necessary, in order to further improve energy efficiency within the HQ building***
- ***Extend the photovoltaic array to increase the proportion of energy generated at our HQ.***

Future development of the Society

The management and Board believe that the Society has weathered the effects of the financial crisis well, and with the extra resources we have taken on, and the work on systems, the Society is in strong shape to continue to grow and develop our activities over the next few years.

Our focus in the coming year will be to increase the volume of sustainable lending which enables us to continue to meet the demand for an ethical savings service. To that end we will continue to strengthen our resources in IT, Communications and our Mortgage and Savings teams.

This will depend to some extent on external factors such as the economy and state of the housing market, but we must also ensure that our capital resources keep pace with the potential for growth. Thus we will continue our preparatory work for capital raising. Delays in the implementation of new international capital rules (due mainly to problems in the Eurozone) have created extra work, and we also find that it is necessary to engage the regulatory authorities to explain the role of social impact investment.

The accumulated reserves of the Society will always be the mainstay of our capital base. Where we deem that supplementary capital can contribute to increasing the pace of growth, our preferred approach is to enable our members to contribute to our capital resources, as is commonplace with other co-operative financial institutions across Europe.

What is very clear is that there are exciting opportunities for the Society coming along in 2013, as we increase our retrofit activity and promote our Fair Green Deal to a wider audience. Thanks to all our members, new and longstanding, in making our work possible in 2012, and we hope to justify your trust in 2013.

Paul Ellis
Chief Executive

25 February 2013

Directors' Report

Introduction

The Directors have pleasure in presenting their Annual Report, together with the Annual Accounts and Annual Business Statement of the Society for the year ended 31 December 2012.

Business objectives of the Society

As stated in the Memorandum adopted in 1998, the Society's principal purpose is making loans which are secured on residential property and are funded substantially by its members.

The advances shall be made in those cases which, in the opinion of the Board, are most likely to promote, encourage or support:

- ***the saving of non-renewable energy or other scarce resources***
- ***the growth of a sustainable housing stock***
- ***the development of building practices, ways of living or uses of land which have a low ecological impact.***

The Memorandum also states that in carrying out its business the Society will promote ecological policies designed to protect or enhance the environment in accordance with the principles of sustainable development.

In relation to its lending activities, therefore, the Society requires any borrower applying for a loan to demonstrate that the purposes for which it is required are consistent with the ecological policies approved by the Board of Directors. This approach to lending is fully in keeping with the original objectives laid down by the Society when it was established in 1981.

Business review

The key performance indicators employed by the Society and the business review for 2012 are discussed within the Chief Executive's Review.

Charitable donations

During the year the Society made charitable donations amounting to £7,261 (2011: £8,401). No contributions were made for political purposes.

Land and buildings

The head office building was valued in 2007 at an open market value of £1,100,000. The carrying book value of the head office at the end of 2012 is £1,190,000. The directors remain of the view that the value in use of the head office is in excess of the carrying value.

The head office building was developed to reflect the ecological business practices of the Society. Where possible recycled and reclaimed materials have been used and energy reduction techniques and practices utilised. Around 7% of the energy used is generated by our photovoltaic cells, with the remainder supplied from renewable sources.

Directors and staff matters

The Society's policy is to not discriminate in any way regarding recruitment, career development and training opportunities. Further, the Society is mindful to consider diversity in its recruitment decisions while keeping business needs to the fore.

The Society is fortunate to have a staff team based around a number of long-serving, committed individuals. It is also unique in that it operates a 5:1 salary ratio, where the largest salary paid does not exceed five times the lowest full-time salary paid.

Mortgage arrears

At 31 December 2012 there were no cases where repayments were 12 months or more in arrears (2011: 5). At the year end there were no properties in possession (2011: 5).

Directors' Report *continued*

Capital

As at 31 December 2012, gross capital amounted to 6.98% of total share and borrowing liabilities, while free capital amounted to 5.74% of total share and borrowing liabilities.

Details of the Society's Basel II disclosures for Pillar 3 are available on the website.

Principal risks and uncertainties

The Society has a documented framework for the management of risk which is subject to continual re-evaluation. Management are responsible for the identification and management of risks facing the Society supported by the risk management function. Risk across the business is controlled as follows:

- the Chief Risk Officer, with the support of the Chief Executive, has overall responsibility for the elaboration of risk systems and mitigation measures with management engagement in risk identification and day-to-day operation of the risk management framework
- the Asset and Liability Committee (ALCO) is primarily responsible for market, liquidity and credit risk (core lending and financial institutions)
- the Board Lending Committee is responsible for new lending initiatives and commercial lending
- business continuity aspects of operational risk are the responsibility of the Technology Manager.

The effectiveness of the Society's Risk Management Framework is monitored and reported on by Internal Audit. Oversight of Risk Management on behalf of the Board is performed by the Risk, Audit, Compliance and Ethics Committee.

Credit risk

Credit risk arises primarily from mortgage lending to individuals, commercial lending to corporate bodies and lending of liquid assets to other financial institutions (counterparties). The Society is exposed to the potential risk that a customer or counterparty will not be able to meet its obligations to the Society as they fall due.

Credit risk arising from mortgage and commercial lending is managed through a comprehensive analysis of both the creditworthiness of the borrower and the proposed security. Following completion the performance of all mortgages and commercial loans are monitored closely and action is taken to manage the collection and recovery process. The risk posed by counterparties is controlled by restricting the amount of lending to institutions without an external credit rating. This control also applies to counterparties with credit ratings below A-.

Market risk

Market risk is the risk that the value of, or income arising from, assets and liabilities change principally as a result of changes in interest rates. The Society's exposure to interest rate risk is limited as it does not engage in fixed rate lending.

Liquidity risk

Liquidity risk is the risk that the Society will be unable to meet current and future financial commitments as they fall due. These commitments include deposits, advances and other borrowings. The approach to management of liquidity risk is described in note 21 to the accounts.

Operational risk

Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. Operational losses can result from fraud, errors by employees, failure to comply with regulatory requirements, equipment failures or natural disasters.

Regulatory risk

The Society will need to replace existing capital instruments as they mature, and is therefore actively seeking new instruments which comply with the forthcoming Basel III capital regime.

Reputational risk

The unique nature of the Society gives rise to a specific form of reputational risk. The Society must ensure that it is clear that it adheres closely to its stated key principles, particularly regarding the ecological basis for its lending programme, in order to continue to justify the trust placed in the Society by the members.

Directors' Report *continued*

Financial risk management objectives and policies

The main financial risks arising from the Society's activities are interest rate risk, credit risk and liquidity risk. The Board reviews and agrees policies for managing each of these risks, of which further detail is provided in note 21.

Suppliers and creditor payment policy

All suppliers are requested to furnish the Society with a copy of their Environmental Policy, and the quality of the documents received forms a part of the approval process.

The Society's policy concerning the payment of its trade creditors is as follows:

- the Society agrees the terms of payment at the start of trading with a new supplier;
- all supplier payments are paid within the agreed terms of payment.

The number of trade creditor days as at 31 December 2012 was 17 days (2011:41 days).

Auditors

The auditors, KPMG Audit Plc, have expressed their willingness to continue in office and in accordance with Section 77 of the Building Societies Act 1986, a resolution for the reappointment of KPMG Audit Plc as auditors is to be proposed at the Annual General Meeting.

When the Society ran a tender process for this work in 2005, we undertook a close examination of the sustainability policies of the candidate firms, and found that KPMG's was by far the best.

Directors

The following persons were directors of the Society during the year:

Malcolm Lynch	*Chair*	Pam Waring	*Secretary*
Paul Ellis	*Chief Executive*	Tony Taylor	*Deputy Chair*
David Black		Steven Round	
Janet Slade	(retired 28 April 2012)	Mark Jones	
Adam Clark	(resigned November 2012)	Helen Ashley Taylor	(appointed 15 May 2012)

Paul Ellis, Tony Taylor and Pam Waring are to retire by rotation and, being eligible, offer themselves for re-election at the AGM.

Helen Ashley Taylor was co-opted on to the Board in 2012 and in accordance with the provisions of Rule 25(4) is required to stand for election at the AGM.

The Board appoint Directors who can offer specific skills and experience to the Society. Helen is a Chartered Certified Accountant with a strong audit background. Over the last twelve years Helen has worked exclusively in the charity and mutual sectors. Helen sits on two professional committees at the Institute of Chartered Accountants and The Association of Chartered Certified Accountants.

The Directors who held office at the date of approval of the directors' report confirm that, so far as they are each aware, there is no relevant audit information of which the Society's auditors are unaware and each director has taken all the steps that they ought to have taken as a director to make themselves aware of any relevant audit information and to establish that the Society's auditors are aware of that information.

On behalf of the Board

Malcolm Lynch
Chair

25 February 2013

Directors' Report on Corporate Governance

Overview

The Society's regulator, the FSA, requires the Board to have regard to the UK Corporate Governance Code issued by the Financial Reporting Council in developing its policies and practices. Although this Code is designed primarily for Listed Companies and not for mutual organisations, such as Building Societies, the Society has adopted its provisions wherever it is appropriate to do so and where it has not done so an explanation is given.

The Board

The Board works with management to set the Society's strategic and policy direction acting in the best interest of its members. It ensures that adequate financial and human resources are in place and it reviews management performance. The Board is responsible for the recruitment and employment terms and conditions of senior management.

The Board has a general duty to ensure the Society operates within the Society's Rules and relevant regulation and legislation and that proper accounting records and effective systems of business control are established, maintained, documented and audited. The Board takes decisions on specific matters such as major capital expenditure, annual budgets, corporate objectives and environmental and ethical issues. The Board maintains a system of effective Corporate Governance and systems of control ensuring accurate and comprehensive business information is produced with sound financial controls and risk management. The responsibilities of Directors in relation to the preparation of the Society's accounts and the statement that the Society's business is a going concern are contained in the Directors' Responsibilities on page 17. The Board meets at least ten times a year.

The Board has a clearly defined schedule of retained powers and has delegated authority in other matters to a number of Board Committees each of which has Board approved terms of reference. Meetings of all Board Committees are minuted and the minutes of each meeting are tabled for consideration at the next Board Meeting. The schedule of retained and delegated powers is reviewed regularly.

All Directors have access to the advice and services of the Secretary who is responsible for ensuring all Board procedures are complied with and advising the Board, through the Chair, on governance matters. The Board has access to independent professional advice, at the expense of the Society, to permit them to discharge their responsibilities as directors. The Society maintains appropriate liability insurance cover in respect of any legal action against its Directors and Officers.

Balance of and appointments to the Board and Independence

All Directors are 'approved persons' and must meet and maintain compliance with the standards of fitness and propriety set down by the Financial Services Authority and comply with the Code of Practice for Approved persons. The Board considers that all its Non-Executive Directors are independent and free of any relationship which could materially interfere with the exercise of their independent judgement. The Board has considered the recommendation within the Corporate Governance Code that Non-Executive Directors stand for annual election after serving a period of nine years, and determined that any Director who has been a member of the Board for nine years will be subject to an internal interview to ensure that they are still independent and if so will be required to stand for annual election. Where a Director who has served nine years is appointed Chair the election period would revert to three years.

The Board has considered the appointment of a Senior Independent Director but feel that the concept of such an appointment is of limited relevance to the Society. One of the main roles of this function is to provide a contact point for members. To meet this, in 2013 the Society will designate a non-executive Member Advocacy Director The precise terms of this function have yet to be determined, but this Director would be the point of contact for members, a channel for members concerns to the Board and its committees, and would seek to ensure the best possible level of membership experience. Until this appointment is made, members who have concerns that they do not wish to discuss with either the Chair or the Executive may continue to contact any member of the Board directly by addressing their correspondence to the individual Director and marking it Private and Confidential, alternatively all Directors attend the AGM and can be approached both before and after the formal meeting.

The Society's rules require that all directors are submitted for election at the Annual General Meeting (AGM) following their appointment to the Board. Where the appointment occurs in the period between the end of the Society's financial year and the AGM itself, they must seek election at the AGM in the following year. Directors are appointed for a three-year term. All Directors are required to seek re-election if they have not been elected at either of the two previous AGMs. Directors may submit themselves for re-election voluntarily.

Directors' Report on Corporate Governance *continued*

The Nominations Committee reviews Board constitution, skills, performance, succession plans and makes recommendations for re-elections of directors. It considers the appointment of new Non-Executive Directors following the circulation of potential vacancies in the Society newsletter. The Committee reviews the skills, knowledge and experience of the candidate against the current requirements of the Board and Society. It evaluates the ability of Directors to commit the time required for their role prior to appointment. Its recommendations are submitted to the full Board for consideration.

Roles of the Chair and Chief Executive

The roles of Chair and Chief Executive are held by different individuals with a clear division of responsibilities. The Chair is responsible for leadership of the board and ensuring the Board acts effectively. The Chief Executive has overall responsibility for managing the Society and implementing strategies agreed by the Board.

Information and professional development

All Directors are encouraged to attend industry events, seminars and training courses to maintain an up to date knowledge of the industry, regulatory framework and environmental issues. All directors have had appropriate briefings on industry issues.

Performance evaluation

Each year Directors are subject to a formal appraisal at which their contribution to the Board's performance is assessed. The assessment includes training, development, and attendance. The Chair and Deputy Chair carry out the Chief Executive's appraisal and the Deputy Chair and an Executive Director appraises the Chair. All other appraisals are undertaken by the Chair.

As required under the UK Corporate Governance Code the Board undertakes an annual evaluation of its own performance and that of its committees.

Risk Management and Internal control and Board committees

The Board is collectively responsible for determining strategies for risk management and control. Senior management have the tasks of designing, operating and monitoring risk management and internal control processes. The system of internal control is designed to enable the Society to achieve its corporate objectives within a managed risk profile. The Board has established committees to give more attention to key areas of the business than is possible within regular Board meetings. The full terms of reference for these committees are available on application to the Secretary.

Risk, Audit Compliance and Ethics committee (RACE)

The principal functions of the Committee are to support the Board in its responsibility for maintaining an appropriate system of internal control to safeguard the funds of both members and depositors and Society assets, including assessments of business risk. The Committee receives regular reports from both the External and Internal auditors. The Internal Audit function provides independent assurance of the effectiveness of the system of internal controls.

As the Society holds that the conduct of its business must result in tangible environmental and social benefits within the context of sustainable economic outcomes accompanied by social justice, it believes that any discussion of risk and internal control must be informed by the Society's understanding of ethics. Therefore the Committee also assesses adherence to our ethical standards, and receives reports from the Ethics Manager.

The Board is satisfied that the Committee has appropriate recent and relevant financial experience to carry out its duties effectively. The Committee is chaired by Tony Taylor. At the invitation of the Chair of the Committee the Chief Executive, Secretary, Compliance Officer and representatives from both Internal and External Audit attend meetings.

The Committee has responsibility for ensuring that effective whistleblowing arrangements are in place. This enables any concerns about any matters whatsoever to be raised by employees in confidence.

The composition and effectiveness of the Committee are reviewed annually by the Board. An induction programme is provided for new RACE members. Membership of RACE is for a period of up to three years, extendable by no more than two additional three year periods. The committee met four times during 2012.

The Committee monitors the independence and effectiveness of Internal and External Audit.

Directors’ Report on Corporate Governance *continued*

Non-audit work undertaken by External Auditors would only be conducted by prior approval of the Risk, Audit, Compliance and Ethics Committee to ensure that the continued independence and objectivity of the Society’s external auditors would not at any time be compromised.

Assets and Liabilities committee (ALCO)

In October 2011 the Board formed ALCO a committee that has taken responsibility for monitoring and controlling structural risks in the balance sheet, liquidity, treasury, funding, recommending policy development and monitoring implementation to ensure that board defined risk limits are adhered to and that the Society has adequate liquid financial resources to meets its liabilities as they fall due.

The responsibilities of this committee were previously held by the full Board, with the creation of the ALCO forming part of the evolution of the Society’s internal arrangements as it continues to grow.

The committee is chaired by the Chief Executive the other members being the Finance Director and two Non-Executive Directors. The committee meets at least six times a year.

Development and Strategy Planning committee (DSPC)

The DSPC is responsible for formulating the future strategy of the Society. The Committee consists of the full Board and is chaired by Steven Round. The committee met three times during 2012.

Board Lending Committee

The Committee examines non-standard risks and non-residential lending proposals. It also reviews potential changes to lending policy and limits. The Committee met twice during the year, and is chaired by David Black.

Nominations Committee

This committee is responsible for reviewing applications for the post of Non-Executive Director and making a recommendation to the full Board. The committee consists of the Chair, one Executive Director and one Non-Executive Director. The Committee met on two occasions in 2012.

The function and details of the **Remuneration Committee** are disclosed within the Directors’ Remuneration Report on page 15.

Board and committee membership and attendance record

Director	Board	Risk, Audit , Compliance and Ethics	DSPC	Board Lending	Remuneration	Nominations	ALCO
Malcolm Lynch	10/11	■	3/3	■	■	2/2	■
Tony Taylor	11/11	4/4	3/3	■	■	1/1	8/8
Janet Slade	4/4	1/1	1/1	■	■	■	3/3
Helen Ashley Taylor	7/7	3/3	2/2	■	■	1/1	■
David Black	10/11	■	3/3	2/2	1/1	■	5/5
Mark Jones	11/11	■	3/3	2/2	1/1	■	■
Steven Round	11/11	4/4	3/3	■	1/1	■	■
Adam Clark	9/9	■	3/3	1/1	■	■	■
Paul Ellis	11/11	3/4	3/3	1/2	■	2/2	8/8
Pam Waring	11/11	4/4	3/3	■	■	■	8/8

The above contains occasional attendance at committee when directors acted as deputies for absent colleagues. The first figure represents the number of meetings attended, and the second the maximum number of possible attendances.

■ *Not a member of this Committee*

Directors' Remuneration Report

Introduction

The purpose of this report is to inform members of the Society about the policy for the remuneration of Executive and Non-Executive Directors. It provides details of the elements of directors' remuneration and explains the process for setting them.

The Society adheres to the FSA Remuneration code which sets out the standards that building societies have to meet when setting pay and bonus awards for their staff. The Code requires disclosure of the fixed and variable remuneration of senior management, risk takers, staff engaged in control functions and any employee receiving total remuneration that takes them into the same remuneration bracket as senior management and risk takers whose professional activities have a material impact on the Society's risk profile. These disclosures are published annually in the Society's Pillar 3 Statement.

Role and composition of the Remuneration committee

The Committee's responsibility is to determine the salaries and fees of the Executive and Non-Executive Directors. In addition, it reviews general salary levels. Consisting of three Non-Executives the Committee meets as required but at least once a year.

Remuneration policy

Non-Executive Directors

Non-Executive Directors receive a fee for their services. Non-Executive Directors do not receive any pension, profit related pay or other taxable benefits. Additional fees are paid to the Chair, Deputy Chair and those Non-Executive Directors who are members of certain Board Committees in recognition of the additional duties and responsibilities associated with these positions. The contribution of each director is appraised annually.

Executive Directors

Remuneration of the Executive Directors comprises a number of elements: basic salary, performance related pay, contributions to the Society's Personal Pension Scheme and other benefits. The Chair appraises Executive Directors annually.

All fees earned by Executive Directors serving on external Boards are paid to the Society.

Basic salary

The Society's policy is for all employees (including Executive Directors) to be remunerated in relation to their expertise, experience, overall contribution and the general market place. The Committee considers external data from salary surveys of comparable institutions. The Society has a long established policy that no basic salary will exceed a maximum of five times the lowest full grade available.

Profit related pay

Executive Directors were historically included in the Society's Profit Related Pay scheme that distributed, on an annual basis, 5% of gross profit (2.5% over £300,000) based on basic salary. This scheme ceased to exist from 1 January 2012 and the final payment based on 2011 profit was paid in March 2012. The scheme is being replaced by a Performance Related Pay scheme, with goals for senior management set by the Board.

Pension

The Society makes contributions equivalent to 8% of basic salary for each member of staff, including Executive Directors, to the Society's Group Personal Pension Plan after an initial service period of 3 months. A death in service scheme is operated which pays a lump sum of four times basic salary. These arrangements apply equally to all qualifying staff, with no enhanced arrangements for Executive Directors or senior management.

Benefits

Executive Directors can participate in the Society's staff mortgage scheme subject to a maximum of £33,000. The Chief Executive is also provided with a company car that can be used by other staff members.

Directors' Remuneration Report *continued*

Contractual terms

None of the Society's Non-Executive Directors have service contracts. Paul Ellis, Chief Executive, has a service contract entered into on 1 December 1999 and Pam Waring, Secretary, has a service contract entered into on 28 December 2001. Both contracts are terminable by either party giving six months notice.

Executive Directors' remuneration

	Salary £000	Profit Related Pay[1] £000	Taxable Benefits £000	Contributions to pension scheme £000	Total £000
2012					
Paul Ellis (Chief Executive)	**72**	**3**	**2**	**6**	**83**
Pam Waring (Finance Director)	**63**	**2**	**1**	**5**	**71**
Totals	**135**	**5**	**3**	**11**	**154**
2011					
Paul Ellis (Chief Executive)	70	2	2	6	80
Pam Waring (Finance Director)	62	1	1	5	69
Totals	132	3	3	11	149

[1] *Profit Related pay relates to the scheme in operation in 2011*

Non-Executive Directors' remuneration

	2012 £000	2011 £000
Malcolm Lynch	**13**	13
Tony Taylor[2]	**14**	10
Janet Slade (Jan – Apr 2012)	**3**	10
David Black	**11**	10
Pamela Parkinson (Jan-Apr 2011)		3
Mark Jones	**9**	10
Steven Round	**9**	8
Adam Clark (Jan – Nov 2012)	**9**	1
Helen Ashley Taylor (May-Dec 2012)	**5**	-
Totals	**73**	65

[2] *Includes additional remuneration in relation to oversight of the Society's Risk function.*

On behalf of the board

Malcolm Lynch
Chair

25 February 2013

Statement of Directors' Responsibilities *in respect of the Annual Report, the Annual Business Statement, the Directors' Report and the annual accounts*

The directors are responsible for preparing the Annual Report, Annual Business Statement, Director's Report and the annual accounts in accordance with applicable law and regulations.

The Building Societies Act 1986 ("the Act") requires the directors to prepare Society annual accounts for each financial year. Under that law they have elected to prepare the Society annual accounts in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice).

The annual accounts are required by law to give a true and fair view of the state of affairs of the Society as at the end of the financial year and of the income and expenditure of the Society for the financial year.

In preparing these annual accounts, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the annual accounts;
- prepare the annual accounts on the going concern basis, unless it is inappropriate to presume that the Society will continue in business.

In addition to the annual accounts the Act requires the directors to prepare, for each financial year, an Annual Business Statement and a Directors' Report, each of which should contain prescribed information relating to the business of the Society.

Directors' responsibilities for accounting records and internal control

The directors are responsible for ensuring that the Society:

- keeps proper accounting records that disclose with reasonable accuracy at any time the financial position of the Society in accordance with the Act;
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Services Authority under the Financial Services and Markets Act 2000.

The directors have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Society and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the society's website. Legislation in the UK governing the preparation and dissemination of annual accounts may differ from legislation in other jurisdictions.

Going concern

In common with many financial institutions, the Society meets its day-to-day liquidity requirements through managing its retail funding sources, and is required to maintain a sufficient buffer over regulatory capital in order to continue to be authorised to carry on its business. The Society's forecasts and objectives, taking into account a number of potential changes in trading performance and funding retention, show that the Society has adequate resources for the foreseeable future. For this reason the accounts continue to be prepared on a going concern basis.

Malcolm Lynch
Chair

25 February 2013

Independent Auditor’s Report *to the Members of Ecology Building Society*

We have audited the annual accounts of Ecology Building Society for the year ended 31st December 2012 set out on pages 19-33. The financial reporting framework that has been applied in their preparation is applicable law and UK Accounting Standards (UK Generally Accepted Accounting Practice).

This report is made solely to the society's members, as a body, in accordance with section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the society'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 society and the society'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 set out on page 17, the directors are responsible for the preparation of annual accounts which give a true and fair view. Our responsibility is to audit, and express an opinion on, the annual accounts 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 (APB's) Ethical Standards for Auditors.

Scope of the audit of the annual accounts

A description of the scope of an audit of annual accounts is provided on the Financial Reporting Council’s website at www.frc.org.uk/auditscopeukprivate.

Opinion on annual accounts

In our opinion the annual accounts:

- give a true and fair view, in accordance with UK Generally Accepted Accounting Practice, of the state of affairs of the society as at 31 December 2012 and of the income and expenditure of the society for the year then ended; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and regulations made under it.

Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

- the Annual Business Statement and the Directors' Report have each been prepared in accordance with the applicable requirements of the Building Societies Act 1986 and regulations thereunder;
- the information given in the Directors' Report for the financial year for which the annual accounts are prepared is consistent with the accounting records and the annual accounts; and
- the information given in the Annual Business Statement (other than the information upon which we are not required to report) gives a true representation of the matters in respect of which it is given.

Matters on which we are required to report by exception

We have nothing to report in respect of the following matters where the Building Societies Act 1986 requires us to report to you if, in our opinion:

- proper accounting records have not been kept by the Society; or
- the annual accounts are not in agreement with the accounting records; or
- we have not received all the information and explanations and access to documents we require for our audit.

Jonathan Holt (Senior Statutory Auditor)
for and on behalf of KPMG Audit Plc, Statutory Auditor
Chartered Accountants
Manchester

25 February 2013

Income and Expenditure Account

for the year ended 31 December 2012

	Note	2012 £000	2011 £000
Interest receivable and similar income	2	**3,818**	3,705
Interest payable and similar charges	3	**(1,749)**	(1,648)
Net interest receivable		**2,069**	2,057
Fees and commissions receivable		**9**	12
Fees and commissions payable		**(25)**	(40)
Other operating income		**57**	66
Total operating income		**2,110**	2,095
Administrative expenses	4	**(1,469)**	(1,317)
Depreciation and amortisation	13	**(81)**	(71)
Provisions for bad and doubtful debts	6	**88**	(94)
Provisions for contingent liabilities and commitments	21	**(53)**	(54)
Profit on ordinary activities before tax		**595**	559
Tax on profit on ordinary activities	8	**(136)**	(134)
Profit for the financial year		**459**	425

The notes on pages 22 to 33 form part of these accounts.

There were no recognised gains or losses other than those reflected in the above income and expenditure account (2011: £nil).

The profit for the year was derived wholly from continuing operations. 'Profit on ordinary activities before taxation' represents the FRS 3 caption 'Operating profit'.

Balance Sheet
as at 31 December 2012

	Note	2012 £000	2011 £000
Assets			
Liquid assets			
Cash in hand		**-**	-
Treasury bills	*10b*	**7,994**	5,994
Loans and advances to credit institutions	*9*	**18,730**	17,793
Debt securities	*10a*	**4,020**	5,082
Loans and advances to customers	*11*		
Loans fully secured on residential property		**67,458**	63,467
Other loans		**9,881**	9,515
Investments			
Other investments	*12*	**174**	122
Tangible fixed assets	*13*	**1,300**	1,359
Prepayments and accrued income		**174**	120
Total assets		**109,731**	103,452
Liabilities			
Shares	*14*	**96,466**	90,175
Amounts owed to other customers	*15*	**5,458**	5,968
Other liabilities	*16*	**379**	364
Accruals and deferred income	*18*	**46**	33
Provisions for liabilities – FSCS Levy	*21*	**124**	105
Provisions for liabilities - other	*17*	**39**	47
Subordinated liabilities	*19*	**1,246**	1,246
		103,758	97,938
Reserves			
General reserves	*22*	**5,973**	5,514
Total liabilities		**109,731**	103,452

The notes on pages 22 to 33 form part of these accounts.

These accounts were approved by the Board of directors on 25 February 2013 and were signed on its behalf by:

Malcolm Lynch
Chair

Paul C Ellis
Chief Executive

Pam Waring
Finance Director

Cash Flow Statement

for the year ended 31 December 2012

	2012 £000	2011 £000
Net cash (outflow)/inflow from operating activities	**(338)**	5,602
Returns on investments and servicing of finance		
Interest paid on subordinated liabilities	**(54)**	(54)
Taxation	**(112)**	(99)
Capital expenditure and financial Investments		
Purchase of tangible fixed assets	**(22)**	(135)
Profit from the sale of fixed assets	**-**	3
Purchase of treasury bills	**(19,003)**	(13,998)
Proceeds from sale of treasury bills	**17,000**	13,498
Purchase of debt securities	**(3,507)**	(6,049)
Proceeds from sale of debt securities	**4,563**	5,052
Purchase of investments	**(52)**	-
Financing:		
Repayment of subordinated debt	**-**	(250)
(Decrease)/Increase in cash	**(1,525)**	3,570
Reconciliation of operating profit to net cash inflow from operating activities		
Operating profit	**595**	559
(Increase)/Decrease in prepayments and accrued income	**(10)**	5
Increase in accruals and deferred income	**73**	138
(Decrease)/Increase in Provisions for bad and doubtful debts	**(463)**	82
Increase in Provision for FSCS levy	**19**	25
Depreciation	**81**	71
Interest on subordinated liabilities	**55**	56
Net cash inflow from trading activities	**350**	936
Movement in:		
Loans and advances to customers	**(3,894)**	(5,221)
Shares	**6,231**	6,717
Amounts owed to other customers	**(510)**	655
Loans and advances to credit institutions	**(2,497)**	2,497
Other liabilities	**(18)**	18
Net cash (outflow)/inflow from operating activities	**(338)**	5,602

Analysis of Decrease in cash	2012 £000	Flows £000	2011 £000
Loans and advances to credit institutions repayable on demand	**8,140**	(1,525)	9,665

Notes to the Accounts

1 Accounting policies

The following accounting policies have been applied consistently in dealing with items which are considered material in relation to the Society's accounts.

Basis of preparation

The accounts have been prepared under the historical cost convention and in accordance with applicable accounting standards. The accounts have been prepared in accordance with the Building Societies (Accounts and Related Provisions) Regulations 1998 ('the accounts regulations') and the Building Societies Act 1986.

Tangible fixed assets and depreciation

Fixed assets are capitalised and stated at cost less depreciation.

Depreciation is provided at rates calculated to write off the cost less estimated residual value of each asset over its expected useful life, on a straight-line basis as follows:

Freehold premises	-	50 years
Computer hardware and associated software	-	3 to 4 years
Equipment, fixtures and fittings	-	4 to 10 years
Motor vehicles	-	4 years
Plant and Machinery	-	10 years

Depreciation is not provided on freehold land in accordance with Financial Reporting Standard 15.

Government grants

Capital based government grants are included within accruals and deferred income on the balance sheet and credited to the profit and loss account on a straight line basis over the estimated useful economic lives of the assets to which they relate.

Leases

Operating lease rentals are charged to the profit and loss account on an accruals basis over the period of the lease.

Provisions and forbearance

Provisions are made to reduce the value of loans and advances to the amount which the directors consider is likely ultimately to be received. Forbearance is exercised where a borrower has personal or financial circumstance that will affect his or her ability to make regular mortgage repayments as they fall due.

Throughout the year, and at the year end, individual assessments are made of all advances and loans on properties which are in possession, in arrears by three months or more, or where due to the borrower's personal and financial circumstances, forbearance has been exercised. The Society, wherever possible, arranges for a concession to be put in place in the form of a payment holiday, or repayment of interest only, for an agreed period of time. Consideration is also given to a borrower in arrears and appropriate arrangements are agreed to under, or overpay, the arrears within an agreed timeframe. Once the agreement has been successfully concluded the case is no longer considered to be impaired but continues to be monitored. Specific provision is made against those advances and loans which are considered to be impaired, whether or not forbearance measures are in place. The small size of the Society's mortgage book enables individual assessment of all forbearance cases. In considering the specific provision for impaired loans, account is taken of any discount which may be needed against the value of the property at the balance sheet date to agree a sale within three months of that date and realisation costs. A general provision is also made against advances which have not been specifically identified as impaired but which the Society's experience and the general economic climate would indicate that losses may ultimately be realised.

Loans and advances in the balance sheet are shown net of all provisions. The charge to the income and expenditure account comprises the movement in the provision, together with the losses written off in the year.

Interest income from all loans is credited to the income and expenditure account as it becomes receivable. Interest on loans which are regarded as impaired is transferred to a suspense account and is not credited to the extent that recovery is considered doubtful.

Notes to the Accounts *continued*

1 Accounting policies *continued*

Pensions

The Society operates a defined contribution scheme for its employees. A contribution of 8% of gross salary is paid into the Group Personal Pension Scheme for all employees after an initial service period of three months.

Taxation

The charge for taxation is based on the profit for the year and takes into account taxation deferred or accelerated because of timing differences between the treatment of certain items for taxation and accounting purposes. Deferred tax is recognised, without discounting, in respect of all timing differences between the treatment of certain items for taxation and accounting purposes which have arisen but not reversed by the balance sheet date, except as otherwise required by FRS 19.

Liquid assets

Debt securities and Treasury Bills are intended for use on a continuing basis in the Society's activities and are classified as financial fixed assets and are stated at cost, adjusted to exclude accrued interest at the date of purchase. Premiums and discounts arising on the purchase of financial fixed assets are amortised over the period to the maturity date of the security. Any amounts so amortised are charged/credited to the income and expenditure account for the relevant financial year. Other liquid assets are stated at the lower of cost (including accrued interest) and net realisable value.

Subordinated liabilities

Premiums and costs incurred in the raising of subordinated liabilities are amortised in equal annual instalments over the relevant period to maturity.

Income recognition

Interest income and fees and commission are recognised on an accruals basis.

Mortgage incentives

Mortgage incentives, such as interest discounts, are charged against interest receivable in the year incurred.

Other investments

Investments are stated at the lower of cost and net realisable value.

2 Interest receivable and similar income

	2012 £000	2011 £000
On loans fully secured on residential property	**3,080**	2,950
On other loans	**472**	428
On debt securities:		
Interest	**95**	124
Amortisation of premiums	**(23)**	(44)
Profit on disposal	**9**	23
On treasury bills at fixed rate interest	**37**	34
On other liquid assets	**146**	188
Other interest receivable and similar income	**2**	2
	3,818	3,705

Notes to the Accounts *continued*

3 Interest payable and similar charges

	2012 £000	2011 £000
On shares held by individuals	**1,615**	1,493
On deposits and other borrowings		
Subordinated liabilities	**55**	56
Other	**79**	99
	1,749	1,648

4 Administrative expenses

	2012 £000	2011 £000
Staff costs		
Wages and salaries	**643**	585
Social security costs	**67**	64
Other pension costs	**48**	48
	758	697
Other administrative expenses	**711**	620
	1,469	1,317
Other administrative expenses include:		
Auditors (exclusive of VAT)		
Audit of the financial statements	**24**	24
Other services pursuant to legislation	**6**	1

5 Employees

The average number of employees (including executive directors) during the year was:

	2012	2011
Full time	**17**	16
Part time	**3**	4
	20	20

Notes to the Accounts *continued*

6 Provisions for bad and doubtful debts

	Other Loans	Loans fully secured on residential property £000	Loans fully secured on land £000	Total £000
At 1 January 2012				
General	-	27	10	37
Specific	-	516	106	622
	-	543	116	659
Income and Expenditure Account				
General	-	(5)	(2)	(7)
Specific	37	(516)	23	(456)
Net Charge	37	(520)	21	(463)
At 31 December 2012				
General	-	22	8	30
Specific	37	-	129	166
	37	**22**	**137**	**196**

The charge shown in the income and expenditure account is made up as follows:

Movement in loss provision (above)	(463)
Losses in year	374
Recoveries of amounts previously written off	1
	88

A provision of £129,000 (2011: £106,000) is included in Specific Provisions made on a Loan fully secured on Land for a mortgage where forbearance has been exercised. There are no provisions for forbearance included in Specific Provision for Loans Fully Secured on Residential Property (2011: nil).

7 Remuneration of and transactions with directors

Total remuneration amounted to £227,000 (2011: £214,000). Full details are given in the Directors' Remuneration Report on pages 15 and 16.

Directors' loans and transactions

At 31 December 2012 there were four outstanding mortgage loans (2011:4), made in the ordinary course of the Society's business to directors and connected persons, amounting to £524,450 (2011: £555,245).

A register of such loans, transactions or arrangements is maintained under Section 68 of the Building Societies Act 1986 and the statement of these details for the current financial year is available for inspection at the Society's registered office by prior arrangement with the Secretary or at the Annual General Meeting.

Notes to the Accounts *continued*

8 Tax on profit on ordinary activities

	2012 £000	2011 £000
Analysis of charge in year at 24.5% (2011: 26.5%)		
Corporation tax on profits of the period	144	111
Adjustment in respect of previous periods	-	(1)
Total current tax	144	110
Deferred tax		
Origination and reversal of timing differences	(8)	24
Total deferred tax (note 17)	(8)	24
Tax on profit on ordinary activities	136	134
Factors affecting current tax charge in year		
Profit on ordinary activities before tax	595	559
Tax on profit on ordinary activities at 24.5% (2011:26.5%)	146	148
Accelerated capital allowances	5	(19)
Short term timing differences	(2)	(7)
Permanent items	7	7
Adjustment to tax charge in respect of previous periods	-	(1)
Small companies rate	(12)	(18)
Current tax charge for year	144	110

In the 2012 Budget on 21 March 2012 it was announced that the UK corporation tax will reduce to 22% over a period of 3 years form 2012. A resolution was passed on the 26 March 2012 for the reduction in the UK corporation tax rate from 26% to 24% (effective from 1 April 2012), and a further reduction to 23% (effective from 1 April 2013) was substantively enacted on 3 July 2012. In the Pre-Budget report on 5 December 2012 it was announced that there will be a further reduction to 21% (effective from 1 April 2014).

This will reduce the Society's future current tax charge accordingly. The deferred tax liability has been calculated based on the rate of 23% substantively enacted at the balance sheet date.

It has not been possible to quantify the full anticipated effect of the announced further 2% rate reduction, although this will further reduce the Society's future current tax chare and deferred tax liability accordingly

9 Loans and advances to credit institutions

Loans and advances to credit institutions are repayable from the balance sheet as follows:

	2012 £000	2011 £000
Accrued interest	40	75
Repayable on demand	8,140	9,665
In not more than 3 months	8,000	6,003
More than 3 months but not more than 1 year	2,500	2,000
More than 1 year but not more than 5 years	50	50
	18,730	17,793

Loans and advances to credit institutions contain no direct exposure to banks domiciled in the Euro zone as at the end of the year.

Notes to the Accounts *continued*

10 Debt securities and Treasury Bills

The directors consider the securities held as liquid assets are held with the intention of use on a continuing basis in the Society's activities and are classified as financial fixed assets rather than current assets. Movements during the year of transferable securities held as financial fixed assets are analysed as follows:

10(a) Debt securities

	2012 £000	2011 £000
Issued by public bodies (listed)	**1,003**	3,077
Issued by other borrowers (unlisted)	**3,017**	2,005
	4,020	5,082
Debt securities have remaining maturities as follows:		
Accrued interest	**16**	22
Repayable in not more than 1 year	**3,002**	4,559
Repayable in more than 1 year	**1,002**	501
	4,020	5,082
Transferable debt securities (excluding accrued interest) comprise:		
Listed	**1,002**	1,520
Unlisted	**3,002**	3,540
	-	-
	4,004	5,060
Market value of listed transferable debt securities	**1,001**	3,057
Included in debt securities are:		
Unamortised premiums	**23**	24

Movements during the year of debt securities held as financial fixed assets are as follows:

Cost (excluding accrued interest	**£'000**
At 1 January 2012	**5,060**
Additions and renewals	**3,507**
Disposals and maturities	**(4,563)**
At 31 December 2012	**4,004**

10(b) Treasury Bills

Treasury bills have remaining maturities as follows:	**£'000**	£'000
Accrued interest	**5**	8
In not more than one year	**7,989**	5,986
	7,994	5,994

Movements during the year of debt securities held as financial fixed assets are as follows:

Cost (excluding accrued interest	**£'000**
At 1 January 2012	**5,986**
Additions and renewals	**19,003**
Disposals and maturities	**(17,000)**
At 31 December 2012	**7,989**

The Society holds one debt security amounting to £1,000,000 with the European Investment Bank. There is no other direct exposure to European debt.

Notes to the Accounts *continued*

11. Loans and advances to customers

	2012 £000	2011 £000
Loans fully secured on residential property	**67,458**	63,467
Loans fully secured on land	**9,840**	9,505
Other loans	**41**	10
	77,339	72,982

Loans fully secured on land include £26,325 of loans which are fully secured on residential property and which were made to corporate bodies, such as Housing Co-operatives, prior to 1 October 1998, the date the Society adopted the powers of the Building Societies Act 1997. The classification of these assets is not consistent with the treatment of similar loans made after 1 October 1998 which are included in 'loans fully secured on residential property' but is necessary to comply with the requirements of the Building Societies Act 1997. The remaining maturity of loans and advances to customers as at the date of the balance sheet is as follows:

	2012 £000	2011 £000
Other loans and advances by residual maturity repayable:		
In not more than 3 months	**723**	1,745
In more than 3 months but not more than 1 year	**2,877**	3,966
In more than 1 year but not more than 5 years	**13,791**	12,671
In more than 5 years	**60,144**	55,259
	77,535	73,641
Less: provisions for bad and doubtful debts (note 6)	**(196)**	(659)
	77,339	72,982

There were 18 accounts (2011: 15) at the end of the year where forbearance is currently exercised equating to 2.14% (2011: 1.7%) of mortgage accounts. The balance of these accounts amounted to £3.001m, (2011: £2.724m) or 3.87% (2011: 3.7%) of the mortgage book. With the exception of one account all Loan to Values on secured loans were less than 75%. Provisions on forbearance cases are disclosed in Note 7.

12. Other investments

The Society holds shares in Mutual Vision Technologies Limited (MVT), which provides IT services to the Society. The Society has an interest bearing loan to MVT of £129,000 (2011: £77,000). The Society also owns 10,000 (2011: 10,000) ordinary shares of £1 in The Phone Co-op Ltd which provides the Society's telephone services. Interest paid by the Phone Co-op is by the issue of further ordinary shares. The Society holds 8,000 ordinary shares in The Ethical Property Company PLC at a purchase price of £9,600. In May 2007 the Society purchased 20,000 shares of £1 in Ecos Fund Limited, an Industrial and Provident Society. The shares held with Ecos Fund Limited were redistributed to Ecos Homes in November 2011. The Society's allocation of shares in Ecos Homes remains at 20,000.

	Shares £000	**Loans £000**	**Total £000**
As at 31 December 2011	45	77	122
Additions	-	52	52
Withdrawal	-	-	-
As at 31 December 2012	**45**	**129**	**174**

Notes to the Accounts *continued*

13. Tangible fixed assets

	Freehold Land & Buildings £000	Plant & Machinery £000	Fixtures, Fittings & Computer Equipment £000	Motor Vehicles £000	Total £000
Cost					
At beginning of year	1,391	126	401	43	1,961
Additions	-	9	13	-	22
Disposals	-	-	(2)	-	(2)
At end of year	1,391	135	412	43	1,981
Depreciation					
At beginning of year	177	99	303	23	602
Charge for year	24	14	35	8	81
Disposals	-	-	(2)	-	(2)
At end of year	201	113	336	31	681
Net book value					
At 31 December 2012	**1,190**	**22**	**76**	**12**	**1,300**
At 31 December 2011	1,214	27	98	20	1,359

Freehold land and buildings, which are included in the balance sheet at cost less deprecation, amounted to £1,190m at 31 December 2012 (2011: £1,214m). Following completion of the meeting room a valuation of the Head Office was carried out on 15 February 2007 by Wilman & Wilman. This valued the freehold land and buildings on an investment method basis at an open market value of £1,100m, which was lower than the carrying value in the accounts. However, the directors consider the value in use of these premises to be in excess of the book value and no provision for diminution in value has been made.

The Society occupies 100% of the freehold land and buildings for its own purposes.

14. Shares

	2012 £000	2011 £000
Held by individuals	**96,466**	90,175
Shares are repayable from the balance sheet date in the ordinary course of business as follows:		
Accrued interest	**669**	609
Repayable on demand	**88,818**	84,356
In not more than 3 months	**2,001**	1,771
In more than 3 months but not more than 1 year	**4,978**	3,439
	96,466	90,175

Notes to the Accounts *continued*

15. Amounts owed to other customers

	2012 £000	2011 £000
Amounts owed to other customers are repayable from the balance sheet date in the ordinary course of business as follows:		
Repayable on demand	**5,208**	5,718
In more than 3 months but not more than 1 year	**250**	250
	5,458	5,968

16. Other liabilities

	2012 £000	2011 £000
Corporation tax	**144**	111
Income tax	**132**	125
Other creditors	**103**	128
	379	364

17. Provisions for liabilities – other

The amounts provided for deferred taxation are set out below:

	2012 £000	2011 £000
At 1 January	**47**	23
Origination and reversal of timing differences	**(4)**	26
Adjustment in respect of prior years	**(1)**	1
Effect of the changes in tax rates	**(3)**	(3)
Charge for the year		
At 31 December	**39**	47

Details of the amounts provided for deferred taxation at 24.5% (2011:26.5%) are set out below:

	2012 £000	2011 £000
Excess of capital allowances over depreciation	**47**	58
Other short term timing differences	**(8)**	(11)
	39	47

18. Accruals and deferred income

	2012 £000	2011 £000
Accruals	**44**	30
Government grants	**2**	3
	46	33

Notes to the Accounts *continued*

19. Subordinated liabilities

	2012 £000	2011 £000
a) Floating rate subordinated liabilities due 2016	**500**	500
b) Floating rate subordinated liabilities due 2019	**750**	750
	1,250	1,250
Less unamortised premiums and issue costs	**(4)**	(4)
	1,246	1,246

The Notes are repayable at the dates stated or earlier at the option of the Society with the prior consent of the Financial Services Authority. All Subordinated Liabilities are denominated in sterling. Interest payments made on the floating rate loan (b) is at a rate agreed with reference to the Bank of England Base. Interest payments on the floating rate loan (a) is at a rate agreed based on the average SVR (Standard Variable Rate) of the top 5 Building Societies. Premiums and discounts, commission and other costs incurred in the raising of Subordinated Liabilities are amortised in equal annual instalments over the relevant period to maturity. Of the Subordinated Liabilities held by the Society, £1.146m is classed as Tier 2 capital resources.

20. Guarantees and other financial commitments

FSCS Levy	**2012 £000**	2011 £000
Balance brought forward	**105**	80
Scheme year 2011/12 Levy paid in year	**(34)**	(29)
Charge for the year	**53**	54
Balance carried forward	**124**	105

In common with all regulated UK deposit-takers, the Society pays levies to the FSCS to enable the FSCS to meet claims against it. The FSCS levy consists of two parts – a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of recoveries it makes using the rights that have been assigned to it. During 2008 and 2009 claims were triggered against the FSCS in relation to Bradford and Bingley plc, Kaupthing Singer and Friedlander, Heritable Bank plc, Landsbanki Islands hf, London Scottish Bank plc and Dumfermline Building Society.

The FSCS meets these current claims by way of loans received from the HM Treasury. The terms of these loans were interest only for the first three years and the FSCS seeks to recover the interest cost, together with ongoing management expenses, by way of annual management levies on members, including Ecology Building Society, over this period.

The Society's FSCS provision reflects market participation up to the reporting date. £86,000 of the provision relates to the estimated management expense levy for the scheme years 2012/13 and 2013/14. This amount was calculated on the basis of the Society's current share of protected deposits taking into account the FSA's estimate of total management expense levies for each scheme year.

The management expenses levy for scheme year 2011/12, which formed part of the provision at 31 December 2011, was calculated using the agreed funding rate of 12 month LIBOR + 30bps. Following the expiry of the initial three year fixed interest term, extensive negotiations between HMT and FSCS resulted in an agreed funding rate of 12 month LIBOR + 100bps which is the rate that will be charged for the HMT loans for the period from 1 April 2012, on which the management expenses levy for scheme year 2012/13 and 2013/14 has been based.

In addition to the management levies, from scheme year 2013/14, triggered by participation in the market at 31 December 2012, the FSCS is to levy over three years the current estimated shortfall on capital loans outstanding of £802m. In common with the management expenses levy, the capital loan repayment was calculated on the basis of the Society's current share of UK protected deposits. The Society has therefore recognised a provision of £38,000 related to the compensation levy.

Notes to the Accounts *continued*

21. Financial risk management

The main financial risks arising from the Society's activities are interest rate risk, credit risk, and liquidity risk. The Board reviews and agrees policies for managing each of these risks, and these are summarised below.

Interest rate risk

The Society is exposed to movements in interest rates reflecting the mismatch between the dates on which interest is receivable on assets and interest payable on liabilities are next reset to market rates. The Society perceives this risk as being minimal.

Interest rate risk exposure

The following table summarises the repricing mismatches as at 31 December 2012. Items are allocated to time bands by reference to the earlier of the next interest rate repricing date and the maturity date.

At 31 December 2012	3 months or less £000	More than 3 months but less than 6 months £000	More than 6 months but less than 1 year £000	More than 1 year but less than 5 years £000	Non-interest bearing £000	Total £000
Assets						
Liquid assets	**21,140**	**4,994**	**4,500**	**50**	**61**	**30,745**
Loans and advances to customers	**77,339**	**-**	**-**	**-**	**-**	**77,339**
Other assets	**10**	**-**	**-**	**164**	**1,473**	**1,647**
	98,489	**4,994**	**4,500**	**214**	**1,534**	**109,731**
Liabilities						
Shares and amounts owed to customers	**101,255**	**-**	**-**	**-**	**669**	**101,924**
Other liabilities	**-**	**-**	**-**	**-**	**588**	**588**
Subordinated liabilities	**746**	**500**	**-**	**-**	**-**	**1,246**
Reserves	**-**	**-**	**-**	**-**	**5,973**	**5,973**
	102,001	**500**	**-**	**-**	**7,230**	**109,731**
Interest rate sensitivity gap	**(3,512)**	**4,494**	**4,500**	**214**	**(5,696)**	**-**
Cumulative gap	**(3,512)**	**982**	**5,482**	**5,696**	**-**	**-**
At 31 December 2011						
Assets						
Liquid assets	20,158	4,532	4,000	50	129	28,869
Loans and advances to customers	72,982	-	-	-	-	72,982
Other assets	10	-	-	112	1,479	1,601
	93,150	4,532	4,000	162	1,608	103,452
Liabilities						
Shares and amounts owing to customers	95,534	-	-	-	609	96,143
Other liabilities	-	-	-	-	549	549
Subordinated liabilities	746	500	-	-	-	1,246
Reserves	-	-	-	-	5,514	5,514
	96,280	500	-	-	6,672	103,452
Interest rate sensitivity gap	(3,130)	4,032	4,000	162	(5,064)	-
Cumulative gap	(3,130)	902	4,902	5,064	-	-

Notes to the Accounts *continued*

21. Financial risk management *continued*

Other assets include fixed assets, investments and prepayments and accrued income. Other liabilities include accruals and deferred income.

Credit risk

All loan applications are assessed with reference to the Society's Lending Policy. Changes to Policy are approved by the Board and the approval of loan applications is mandated. The Board is responsible for approving treasury counterparties.

Liquidity risk

The Society's Policy is to maintain sufficient liquid resources to cover cash flow imbalances and fluctuations in funding to retain full public confidence in the solvency of the Society and to enable the Society to meet its financial obligations. This is achieved through maintaining a prudent level of liquid assets, and through control of the growth of the business. The Society's liquid assets are currently entirely composed of retail funds, without recourse to wholesale funding. As a prudent measure in light of the "credit crunch", the maturity profile of the Society's liquid assets has been shortened, and a wider range of counterparties among banks and building societies has been adopted.

22. General reserves

	2012 £000	2011 £000
At beginning of year	**5,514**	5,089
Profit for the financial year	**459**	425
At end of year	**5,973**	5,514

23. Pensions

The amount charged during the year for individual pension schemes in respect of staff was £47,810 (2011: £48,129). There were no contributions owing to these schemes at 31 December 2012. (2011: £77).

Annual Business Statement

Year ended 31 December 2012

1 Statutory percentages

	Statutory limit	**At 31 December 2012 %**	At 31 December 2011 %
Lending limit	25.00	**13.36**	13.36
Funding limit	50.00	**5.35**	6.21

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986.

The lending limit measures the proportion of business assets not in the form of loans fully secured on residential property.

The funding limit measures the proportion of shares and borrowings not in the form of shares held by individuals.

The statutory limits are as prescribed by the Building Societies Act 1986 and ensure that the principal purpose of a building society is that of making loans which are secured on residential property and are funded substantially by members.

2 Other percentages

	2012 %	2011 %
Gross capital as a percentage of shares and borrowings	**6.98**	7.03
Free capital as a percentage of shares and borrowings	**5.74**	5.66
Liquid assets as a percentage of shares and borrowings	**30.16**	30.03
Profit after taxation as a percentage of mean total assets	**0.43**	0.43
Management expenses as a percentage of mean total assets	**1.45**	1.39

Gross capital represents the general reserves and subordinated liabilities. Of the subordinated liability shown on the balance sheet £1.146m is classed as capital.

Free capital represents the gross capital less tangible fixed assets plus general mortgage loss provision as shown in the balance sheet.

Shares and borrowings represent the total of shares and amounts owed to other customers, including accrued interest.

Liquid assets are taken from the items so named in the balance sheet.

The profit after taxation is the profit for the year as shown in the income and expenditure account.

Management expenses are the administrative expenses plus depreciation and amortisation for the year as shown in the income and expenditure account.

Mean total assets are the average of the 2012 and 2011 total assets.

Annual Business Statement *continued*

Year ended 31 December 2012

3 Information relating to directors and other officers at 31 December 2012

Name and Date of Birth	Occupation and Date of Appointment	Other Directorships
Malcolm John Lynch 29.4.55	Solicitor 24.7.1998	The Trust for Education Leeds Youth Opera
Paul Charles Ellis 10.9.57	Building Society Chief Executive 5.5.1984	Mutual Vision Technologies Ltd Passivhaus Trust INAISE (International Association of Investors in the Social Economy)
Pam Waring 12.6.56	Building Society Finance Director and Secretary 7.6.2000	
David Black 27.12.42	Housing Finance Consultant 15.6.2000	Hideaway Youth Project Addiction Dependency Solutions
Peter Anthony Taylor 27.7.51	Retired Building Society Executive 27.01.2006	The Forget Me Not Children's Hospice Ltd FMNT Trading Ltd Ecology Building Society Charitable Foundation Ltd
Mark Robert Jones 01.03.59	Engineer 01.03.2008	Ecology Building Society Charitable Foundation Ltd
Steven John Round 08.04.60	Management Consultant 09.12.2010	Strategic Intent Ltd The Big Issue Foundation London Rebuilding Society Limited
Helen Ashley Taylor 13.12.65	Accountant 15.05.2012	

Paul Ellis and Pam Waring both have service contracts, details of which can be found in the Directors' Remuneration Report on page 16.

Documents may be served on the above directors and should be marked 'private and confidential' c/o Financial Services Audit, KPMG Audit Plc, St James Square, Manchester, M2 6DS.

Officers

George Haslem	*Chief Operating Officer*
John Ainley	*Compliance Manager*
Jon Lee	*Business Development Manager*
Richard Saville	*Technology Manager*
Anna Laycock	*Communications and Research Manager*