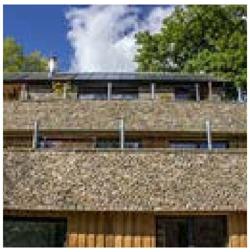
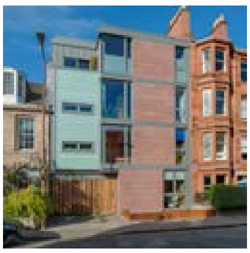
Ecology
Building Society

# Annual Report & Accounts

31 December 2017



## Building a greener society

# Contents



**Registered office**

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# Chair's statement

> **Our members push us to be innovative and make real change.**

**Your Society has delivered another strong financial performance in 2017, with an increase in total assets to more than £178m and maintenance of our profitability. This allows us to continue investing to support Ecology's future growth, as we work towards delivery of our vision of building a greener society.**

We began the year with the ongoing regulatory uncertainty regarding future capital requirements for key elements of our sustainable lending portfolio, which had limited much of our lending activity to those projects that achieve the greatest gains in terms of carbon reductions. Whilst the position was resolved early in 2017, it was evident that the impact of our actions to reduce lending would continue into the year and this has resulted in a reduction in total mortgage lending and mortgage assets. We are planning for growth in the coming year and anticipate that our mortgage lending will increase once again.

As a mutual, Ecology is powered by its members. I was very pleased to welcome members to our AGM and Members' Meet-up in Bristol as well as our regional Members' Meet-ups in London and Manchester where we discussed how we are offering an inspiring alternative for people who believe in the positive potential of a fair and transparent financial system.

Our members have enabled us to achieve this by sharing their ideas and feedback, pushing us to be innovative and make real change and, in late 2017, we launched our Member Survey. The results will provide insight into members' experience of our services and enable them to share thoughts about our mission and values. Our last survey, in 2012, has helped to define Ecology's vision over the last five years. We had a strong response rate from members this year – I would like to thank everyone for their continued support and engagement. We are currently working through the responses and will share the outcomes of the survey later this year.

I am thrilled that the Society was recognised twice in the Mortgage Finance Gazette (MFG) awards, which celebrate innovation and achievement in our sector. Paul Ellis was the winner of MFG's Leadership award. Already the longest serving CEO in the UK building society sector, in 2017 he celebrated a quarter of a century at Ecology. I am immensely proud that Paul's outstanding contribution to sustainable finance over 25 years has been recognised. His work serves as an inspiring example of the power of values-based leadership and its role in transforming the financial system.

MFG also recognised Ecology for our pioneering work to provide mortgages for permanently affordable homes in London. Through this and our long-standing commitment to the sector I believe we are cementing our place as a leading supporter of community-led approaches, which are helping people take back control of housing. Our support for initiatives such as these, as well as our wider support for sustainable lending, demonstrates how Ecology can be a disruptive enabler of practical, visionary ideas.

The Board exists to ensure appropriate corporate governance of the Society and it's important that it has the right mix of skills and experience to scrutinise and provide critical challenge to the Executive, while upholding Ecology's ethics and environmental mission. I am, therefore, delighted to have welcomed a new non-executive director, Vince Smith, to the Board. Vince, who will be standing for election this year, brings strong corporate treasury experience to the Board as well as his passion for the environment and sustainability.

During 2017 the Board asked me to conduct a review, on a consultancy basis, to harness the power of new technologies. My review highlighted the need for the Society to further invest so that we can take advantage of modern and effective digital ways of working – not just for the immediate future but to give Ecology a long-term platform for the development of new products and services for our members. Over time, this will enable us to improve the way we support and engage with members and help us reach a wider audience while continuing to build our resilience.

It only remains for me to thank the Board and the Ecology staff team for their continued commitment and hard work in pursuit of our environmental and social objectives.

**Steve Round**
*Chair*
2 March 2018

# Chief Executive's review

**Delivering consistently healthy financial results is, of course, essential for the security and stability of any business. I am pleased that we can report another strong financial performance with continued profitability and an increase in assets underpinned, again, by record levels of savings balances.**

During 2017 we experienced a 3% reduction in our total mortgage balances. Early in the year we received the good news that the uncertainty regarding potential changes to regulatory requirements for capital relating to key aspects of our sustainable lending programme had been resolved. This uncertainty had constrained our lending volumes for a considerable period in 2016 and it has required significant time and effort to rebuild the 'pipeline' of potential mortgage funding opportunities, while adhering to our core principles in the pursuit of sustainability. Good progress was made during 2017 and we are confident that the current pipeline along with new projects will restore strong and positive growth to our mortgage book in 2018. This rebuilding process also coincided with an increase in mortgage redemptions as many of the record number of projects we supported in 2015 reached the completion of their construction period and some borrowers were able to repay their mortgages, contributing to the reduction in overall mortgage assets.

We continue to experience high levels of liquidity and it remains important to carefully balance the needs of our savers and borrowers. Therefore, following last November's Bank of England base rate increase, we decided to leave savings and mortgage rates unchanged. The continuation of central bank support for schemes such as Funding for Lending has caused savings rates, in the wider market, to remain suppressed and supported ultra-low rates for mainstream mortgages. However, as these schemes finally close and their effects begin to unwind, we will keep all rates under constant review so that we can continue to support both savers and borrowers. Despite the high levels of liquidity we were pleased to be able to start accepting applications for our Regular Savings account in October. This enabled us to welcome new members to the Society while limiting the potential inflows due to the maximum monthly subscription.

> *"Good progress was made during 2017 and we are confident that the current pipeline along with new projects will restore strong and positive growth to our mortgage book in 2018."*

We have also invested in systems, processes and capability to support future growth and enhance the member experience. During 2017 we bolstered our communications, IT and compliance functions as well as recruiting a HR manager. Strengthening these teams provides a firm foundation for the modernisation and growth of the Society while improving services for members. Our people are critical to helping us deliver our plans and I would like to thank the team for their continued support and commitment in maintaining our high ethical and service standards.

During the year I marked my 25-year anniversary at Ecology, which provided a moment to reflect on what has been achieved during that time. There have been so many successes over the years: we broke the traditional rules of mortgage pricing with our C-Change discounts, which incentivise borrowers to improve the environmental performance of their home; our eco-build office in Silsden, West Yorkshire, was recognised as one of the ten most sustainable 'bank' headquarters in Europe; as founding members of the Passivhaus Trust we helped drive the uptake of the Passivhaus low-energy concept in Europe; we were also told by a leading commentator that our lending was instrumental in kick-starting the demand for green building products in the UK.

I am especially proud that, in November, Ecology supported the first ever National Community-led Housing Conference. This was the biggest event the sector had ever seen and provided an opportunity to showcase our award-winning support for the London Community Land Trust's affordable homes. I addressed a packed audience, explaining our desire to support the growth in community-led housing. It was a real privilege to be part of such an amazing day, making history and hearing inspiring and innovative stories of people-powered housing. I believe that Ecology has an exciting and prominent role to play in helping to develop the sector.

Addressing the energy efficiency of our existing housing stock remains a priority if we are to meet the UK's carbon reduction targets. We continue to champion innovative, energy-efficient build systems including lending to projects involving off-site construction. We also supported the SuperHomes Open House events in September, enabling a record 106 SuperHome openings. The Open House events provide honest and practical advice to those considering undertaking energy efficiency improvements. In addition we are supporting the Carbon Co-op programme of home energy efficiency training in the North West of England. We recognise that we have an important role to play in assisting those organisations that promote and raise awareness of the benefits of environmental improvements.

A summary of the main key financial performance indicators (KPIs) used by the Board, along with a more detailed commentary on our progress is given in the Strategic Report (pages 6-9), as well as a summary of how our operations impact on the environment and the wider community.

## Future development of the Society

During 2017, the populist and anti-establishment sentiment which had emerged the previous year continued unabated and the world remains an uncertain place. The environmental gains of the global consensus to tackle climate change were undermined by the, not unexpected, withdrawal of the United States from the Paris climate change treaty and there is continued lack of clarity about the United Kingdom's future relationship with the European Union.

However, in the face of these challenges, I am glad to report there are positive signs of a growing interest in our lending model and, over the summer, we were pleased to join with other Global Alliance for Banking on Values (GABV) members to help inform the emerging work of the European Union (EU) on sustainable finance.

Closer to home, the launch of the UK's Clean Growth Plan demonstrated that the Government recognises the challenges we face in moving to a low carbon future. While the plans themselves need to move beyond statements of ambition to practical policies that deliver, we will continue to actively engage with policy makers to highlight our experience of sustainable lending. We believe that the combination of the emerging interest in sustainable finance and the apparently steadfastly resilient UK economy will present opportunities for us to grow our environmental and social lending in 2018.

We will be developing our capability to source this new lending by working with many of our partner organisations to extend our reach while adhering to our ecological commitments. We plan to further develop our support for community-led housing given the sector's potential to help tackle the housing affordability crisis.

Following the launch of our new website in 2016 we have continued to prioritise the development of our online and digital capabilities. I was particularly pleased that, in the run-up to our AGM in Bristol, a majority of votes cast, were cast online for the first time, demonstrating how new technologies can help members to become involved in our work as well as helping to reduce our costs and our paper use. There are plans for significant investment in infrastructure and digital capability that will enable the Society to thrive in a modern environment, improve engagement with our members and share our message with a wider audience.

I would like to thank all members for your support throughout the year and we look forward to delivering another year of sustainable growth in 2018.

**Paul Ellis**
*Chief Executive*
2 March 2018

# Strategic report

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.

The Chief Executive's Review on pages 4 to 5 provides an overview of the Society's performance during 2017 which should be read in conjunction with this report.

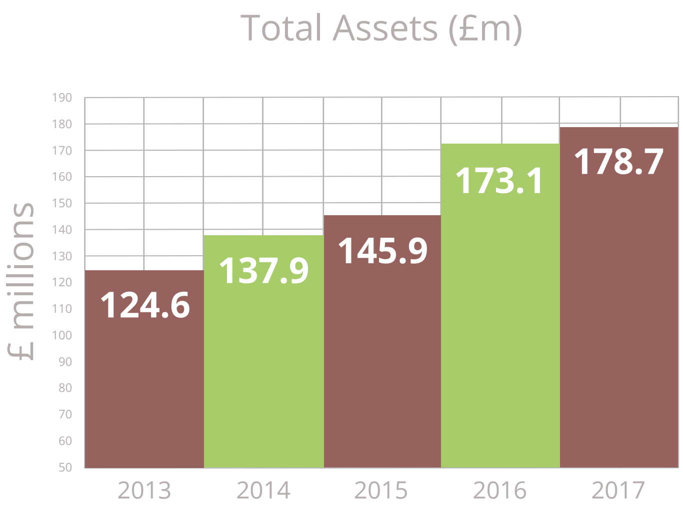
The Board uses a number of Key Performance Indicators (KPIs) to measure the performance and position of the Society on a regular basis. This section provides more detail on these KPIs and the table below provides the actual position as at the end of the current and preceding two years.

## Key Performance Indicators

| | **2017** | 2016 | 2015 |
|---|---|---|---|
| **Total assets** | **£178.7m** | £173.1m | £145.9m |
| **Mortgage asset growth** | **-3.03%** | 3.94% | 24.29% |
| **Mortgage lending** | **£28.2m** | £30.7m | £42.1m |
| **Savings balances** | **£167.8m** | £163.1m | £134.7m |
| **Liquid assets as a % of shares and borrowings** | **36.14%** | 31.77% | 21.83% |
| **Management expenses as a % of mean total assets** | **1.42%** | 1.45% | 1.46% |
| **Net profit** | **£0.915m** | £0.920m | £0.881m |
| **Profit after taxation as a % of mean total assets** | **0.52%** | 0.58% | 0.62% |
| **Core Tier 1 capital** | **£9.538m** | £8.594m | £7.736m |
| **AGM – voting turnout** | **16.17%** | 15.92% | 16.54% |

## Asset growth

The Society has continued to actively manage savings inflow during 2017 and as a result Total Assets increased only moderately by £5.6m to £178.7m (2016: £173.1m), in percentage terms 3.2% (2016: 18.59%). An excessive level of unutilised funding represents a cost to the Society and does not contribute to its sustainable lending programme. **The Society does not pursue growth for its own sake, rather we view growth as a sign of our success in meeting the needs of our savers and supporting our borrowers to build, renovate or buy sustainable properties.**



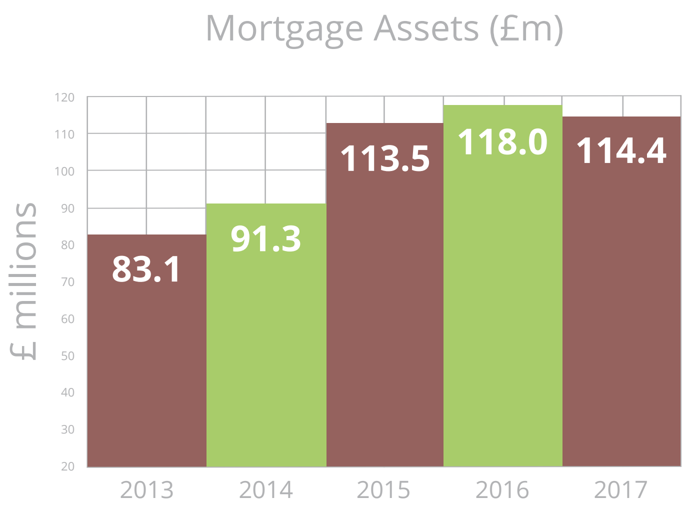

## Mortgages

Whilst gross lending levels for the year were only slightly lower than expected, there was a requirement to rebuild the pipeline of new mortgages during a period of inflated redemption activity resulting from the high lending volumes in 2015. As projects moved from the construction phase to completed phase and the two-year early repayment charge period ended, some borrowers have repaid some, or all, of their mortgage and others have taken advantage of the exceptionally low fixed interest rates available in the wider market, over the last 12 months. This has resulted in a modest reduction in mortgage assets of -3.03% (2016: 3.94%). Gross lending for the year is recorded as £28.2m (2016: £30.7m). The movement in mortgage assets reflects gross lending less redemptions, repayments and effective interest rate adjustments. Having considered the Bank base rate increase in November, the Society decided to hold mortgage interest rates at the previous level. This action was taken to enable ongoing support for more projects delivering a positive environmental or social benefit.

**By the year-end, over 42% (2016: 32%) of loans outstanding were benefiting from one of our C-Change discounts, which reward work undertaken on the property to help combat climate change – showing that the rapid growth in 2014-2015 mortgage lending was not at the expense of environmental quality.** The increase on the previous year reflects our focus, in recent years, on lending for projects such as self-build, which typically attract a C-Change discount. The discount is applied following confirmation of the energy rating achieved.

At 31 December 2017, there were no cases, in possession, or 12 months or more in arrears (2016: nil). In certain circumstances the Society exercises forbearance to assist borrowers who are experiencing financial difficulty, for example, agreeing to interest only payments on a temporary basis. In each case an individual assessment is made to ensure that it is in the best interests of the borrower and the Society. At 31 December 2017, there were 14 cases (2016: 16) under forbearance with total balances of £2.945m (2016: £2.690m) and arrears totaling £5,336 (2016: £204).

Total held provisions against possible mortgage losses reduced to £624,000 (2016: £662,000). Provisions held continue to include two cases which are not in arrears but where Society management are working with our borrowers to navigate difficult operating conditions.




## Savings and liquidity

Savings balances consist of shares and amounts owed to other customers. At the end of 2017 the total savings deposited with the Society grew by 2.9% reaching £167.8m (up from £163.1m at the end of the previous year). In 2016 the Society took action to reduce the volume of savings in response to the requirement to constrain lending activity. During the year there has been an increasing demand from prospective new members who wish to save with the Society. As a result, in October we opened up the Regular Savings account to new members. This has the benefit of enabling the Society to welcome new members but savings inflow is controlled due to the relatively low monthly deposit limit. At the year-end liquidity levels were at a significantly higher level of 36.14% (2016: 31.77%). **We aim to restrict the amount of funding that is not lent out to ensure that the majority of savers' funds are creating value in the real economy. We see our role as providing a savings service for those who wish to invest in pursuit of social and environmental goals, preferring where possible to source our funds for lending direct from individuals and community groups supportive of our mission, rather than taking in wholesale money from other financial institutions.**

We maintained our rates during the sustained period of unprecedented low interest rates and reductions in the market for similar accounts. Our savings rates continue to remain competitive in the ethical savings market and therefore following the Bank of England's decision to increase the base rate in November 2017 we made no adjustment to our savings rates. Interest rates will remain under review during 2018.

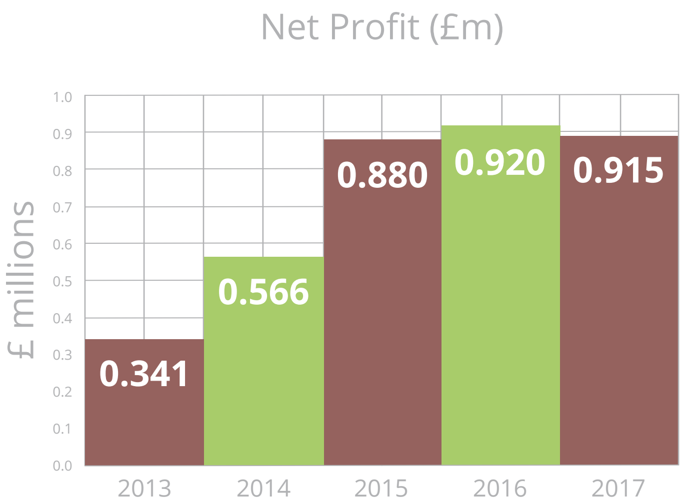
## Management expenses

The cost base of the Society grew by 8.37% (2016: 11.03%) and the higher level of overall asset growth meant that the management expenses ratio at 1.42% was slightly lower than the previous year (2016: 1.45%). **Wherever possible, we use the most sustainable and ethical option when purchasing goods and services. In some cases we accept that we will pay more than for the less sustainable option. In 2017, this added 3.53% to our costs – without this the management expenses ratio would have been 1.37%.**

## Profit and capital

Net profit for the year amounting to £0.915m (2016: £0.920m) was added to the general reserves, which now total £9.595m (2016: £8.680m). This profit acts as a buffer against adverse market movements or changes in the economic conditions.

At 31 December 2017, the ratio of gross capital as a percentage of total share and deposit liabilities was 5.85% (2016: 5.53%) and free capital was 5.16% (2016: 4.76%). The increase in the ratios is as a result of the low increase in savings levels.




In addition to measuring the size of capital resources relative to assets it is important to measure asset size relative to the risk of assets on the balance sheet. The Core Tier 1 solvency ratio measures the ratio of Society reserves against risk weighted assets calculated under Capital Requirements Directive IV (CRD IV). In the case of the Society this is under the standardised approach to credit risk which uses standard risk weights and places no reliance on internally developed capital models. At the end of the year Core Tier 1 ratio stood at 18.05% (2016: 16.98%). The ratio has increased in the year by 1.07% on a like-for-like comparative basis in line with the increase in the capital requirement relative to capital resources in comparison to 2016.

The leverage ratio increased by 0.24% to 5.14% (2016: 4.90%) as a result of low total asset growth in the year. The leverage ratio expresses Tier 1 Capital as a percentage of total assets plus mortgage impairments plus a proportion of mortgage pipeline commitments.

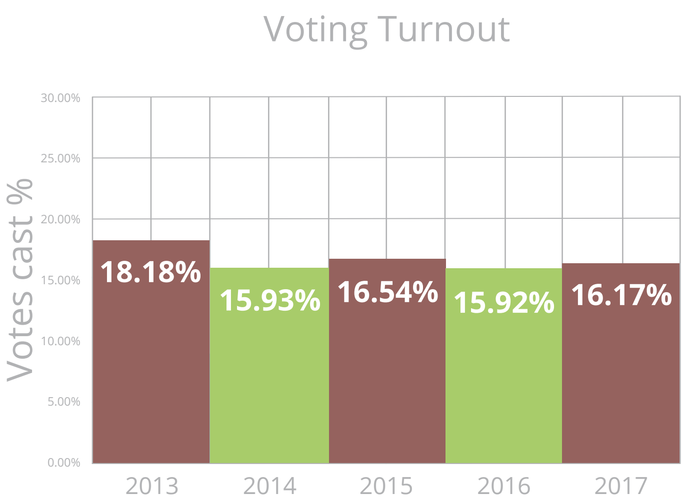
The level of profit we are currently making is sufficient to ensure that we maintain the required level of capital to underpin our current growth based on existing capital requirements.

The Board complies with the Capital Requirements Regulation (CRR) which requires the Society to assess the adequacy of its capital through an Internal Capital Adequacy Assessment Process (ICAAP). Scenario analysis and stress testing is performed on key business risks to assist the Board in assessing whether the Society could survive a severe economic downturn and other severe business shocks.

Through the application of the ICAAP, the Board is satisfied that the Society holds sufficient capital to satisfy both the CRD's Pillar 1 requirements and to cover those risks that the Board has identified under Pillar 2. The Pillar 3 disclosures, including the Pillar 2A percentage and figure, required by the CRD are available on the Society's website: **ecology.co.uk**.

## Member relations

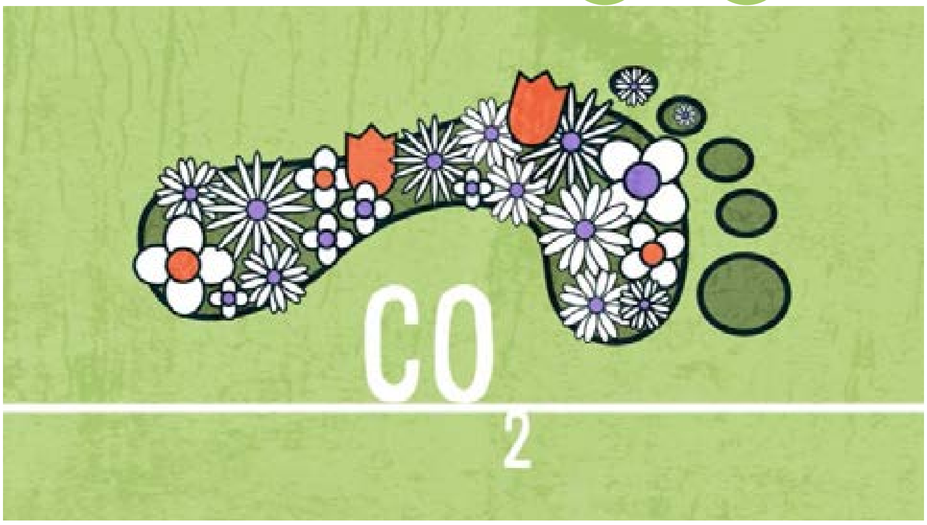
In 2017, our AGM and Members' Meet-up was held at The Station, a community venue in Bristol where members heard from sustainable borrower and CEO of the Association for Environment Conscious Building (AECB), Andy Simmonds, who shared experience of the retrofit of his family home to Passivhaus EnerPhit standard. Members also heard from Bristol Pound co-founder, Chris Sunderland, about plans for a community food centre. Voting turnout increased slightly on the previous year and we continued to explore ways to increase member engagement including completing our pilot programme of regional Members' Meet-ups, held in London and Manchester. These provided a forum for members to input into our support for community-led housing and energy-efficient whole home retrofit respectively.




*Ecology-backed project, Bath Street Collective Custom Build*

# Our positive impact

Ecology exists to support projects and people that are delivering benefit for society and the environment. In short, we want to build a greener society through enabling the positive power of finance. Here, we give a snapshot of Ecology's recent impacts, from the carbon footprint of our business operations, to ways that we're supporting sustainable development in the UK and further afield, looking at where we're getting it right and where we can improve.




## Supporting energy efficiency

We want to help as many people as possible to improve the energy performance of their properties. Energy-efficient buildings mean reduced demand for natural resources and lower bills for residents. The majority of Ecology-backed projects are achieving their target energy rating and – with almost 77% achieving EPC B or above – are well ahead of the England average, which the 2016-17 *English Housing Survey* states as EPC D. Looking ahead, we want to help an even greater proportion of our borrowers to achieve their energy-efficiency goals.

In 2017 we supported the SuperHomes Open House events. SuperHomes is a national network of over 200 homes, which have all reduced their carbon footprint by a minimum of 60%. Our support enabled a record 106 SuperHome openings, with 422 people registered to attend the visits.

We also supported the regional Carbon Co-op programme of home energy efficiency training in the North West of England which will be continuing throughout 2018. The sessions give expert advice on transforming properties into efficient low-carbon homes.

## Backing renewable energy

Sustainable investing isn't just something we encourage others to do – we ensure our own investments are contributing to the world in a positive way and having a meaningful impact. In 2017, Ecology invested £490,000 in two renewable energy projects via sustainable investment platform, Abundance.

**Atlantis Ocean Energy** is developing a tidal stream energy system in the UK. It is estimated that tidal stream energy has the potential to generate 11GW of electricity in the UK alone, equivalent to two-and-a-half-times the production of Hinckley Point C. Ecology investment: £250,000

**United Downs Geothermal** aims to develop the first UK geothermal power plant. Based in Cornwall, the plant will deliver commercial-scale electricity generation using the heat naturally generated by the region's granite bedrock. Ecology investment: £240,000

Pre-2017, we invested in a variety of other Abundance projects, including a scheme to install solar PV systems on social houses in Berwickshire and the construction of a single Enercon E48 wind turbine in Aberdeenshire.

We have also invested in other organisations and funds that support our mission, including Co-operative and Community Finance (CCF), which supports enterprises in disadvantaged communities.

## Shrinking our carbon footprint

We want to shrink the amount of carbon associated with our operations. We aim to do this through improving resource efficiency, increasing recycling, encouraging employees to use sustainable means of transport, and producing our own renewable energy. Ecology's office has an electric car charging point, photovoltaic (PV) panels, a sedum roof and a mechanical ventilation heat recovery system (MVHR). We measure our carbon footprint and in 2016 (the most recently available) this increased slightly to 11.2g $CO_2$ per £ of new lending (2015: 11g $CO_2$ per £ of new lending).

We are continuing to explore ways that we can reduce the carbon output of our activity, both by minimising emissions in the first instance and, as a secondary measure, supporting carefully selected offsetting schemes.

## Reducing our paper use

We are continuing to look at ways of reducing our paper use. This includes reducing both the amount of paper used at our head office as well as the paper we send to members in mailings. For example, in 2017 we reduced the amount of paper used for the AGM mailing by 9.1% as more members chose to receive their AGM packs by email. In addition the easiest way to take part in our Member Survey was online, with the option to complete a paper survey.

## Paying responsibly

We make sure that we reward people fairly. As an accredited Living Wage employer, all Ecology staff are paid a fair wage – a policy that extends to contractors working on our premises. We also stipulate that no basic salary will exceed eight times the lowest full grade salary.

Our responsible approach to pay doesn't end with our employees – it extends to how we pay our taxes. In 2016 Ecology became the first UK building society to be awarded the Fair Tax Mark. This independent accreditation demonstrates our genuine commitment to be open and transparent about our tax affairs, and to do the right thing when it comes to paying taxes.

## Leading the field

In recognition of his bold and committed leadership, Ecology CEO, Paul Ellis, was awarded the Leadership award at the 2018 Mortgage Finance Gazette Awards. The longest-standing CEO of any UK building society, Paul recently celebrated 25 years with Ecology and 22 years as CEO. His work serves as an inspiring example of the power of values-based leadership.

## Commercial sponsorship

Ecology also attended and sponsored a variety of industry events, including the first national Community-led Housing Conference, the Ethical Consumer Conference and the Carbon Co-op's retrofit training programme. During 2017, we gave a total of £23,010 in sponsorship to events and programmes supporting our mission to build a greener society.

> *"Thanks to Ecology, families have now been able to move into a genuinely affordable home that will remain affordable to benefit local people for generations to come."*
>
> - Catherine Harrington, Director, National CLT Network

## Encouraging innovation

Ecology's partnership with the London Community Land Trust (CLT) has enabled a unique mortgage solution for residents of the CLT's affordable housing scheme at St. Clements, Tower Hamlets. The development includes 23 affordable homes, the sale price of which are coupled to local earnings rather than open market value, ensuring the homes remain permanently affordable. In recognition of this pioneering work, Ecology was presented with the Mortgage Product Innovation award at the 2018 Mortgage Finance Gazette Awards.

## Enabling people-powered housing

Ecology continues to champion community-led housing projects that promote social well-being, economic resilience and environmental sustainability. Recent Ecology-backed projects include Bath Street Collective Custom Build in Edinburgh. Occupying a previously vacant urban plot, the newly built four-storey building is home to families from the local area of Portobello. Residents collectively manage the property, which was designed to Passivhaus-equivalent levels of energy efficiency and is powered entirely by renewables.

### Building networks

Ecology doesn't stand alone. We're part of a global community of organisations striving for a greener society. We carefully consider our relationship with these networks so that we can understand how we are helping to strengthen them as well as how they are adding value to our own operations.

### Investors in the Environment (iiE)

Since August 2014, Ecology has been a member of iiE – a national environmental accreditation scheme designed to help organisations reduce their impact on the environment. In the last three years, we've secured the highest achievement, the Green Award. This reflects Ecology's work in minimising our negative impact on the environment, not only through our lending, but through our own actions.

## We're proud to have connections with:


### Global Alliance for Banking on Values (GABV)

We're a member of GABV – an independent network of banks using finance to deliver sustainable development. GABV assesses members on a set of key metrics designed to guide the development of a values-based approach to finance. These include a **triple bottom line approach** and support of the **real economy**:

**Triple Bottom Line**

GABV states that a triple bottom line approach of people, planet and prosperity should be at the heart of the business.

In 2017 we reported that 63.4% of our lending has brought about benefits to the environment or supported social developments. The remaining 36.6% represents mortgage cases that have taken over two years to achieve their objective and so the benefits are yet to be realised.

**Real Economy**

GABV emphasises that business should be grounded in communities, serving the real economy.

In 2017 69.2% of our lending and investment supported the real economy. The remaining 30.8% is invested in the financial economy to ensure we meet certain regulatory requirements; these investments include liquidity deposits held with other banks and building societies, and mortgage-backed securities for low income housing.

## Upholding the Sustainable Development Goals (SDGs)

In September 2015, countries from all over the world came together and agreed to adopt a set of goals that would end poverty, protect the planet and ensure prosperity for all. Achieving these goals requires that governments, the private sector, civil society and individuals all do their part.

The mission of Ecology is aligned with many of the SDGs and we continue to consider how our work can support them. Being a partner of organisations like UK Stakeholders for Sustainable Development (UKSSD), which is working to facilitate delivery of the SDGs in the UK, helps us to consolidate our efforts toward supporting the goals and to ensure we're part of the global conversation around their success.

# 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 2017.

## Business objectives

Information on the business objectives of the Society are detailed in the Strategic Report on pages 6 to 9.

## Principal risks and uncertainties

The risks faced by the Society are similar to those involved in running any financial services business: competition, the cost of regulatory compliance and statutory requirements, business retention, pressure on margin and risks from changes in the wider economy.

The Society sets a risk appetite which helps to protect members' interests and reduce exposure to the principal risks and uncertainties facing the business.

The Society has developed a risk management framework that is designed to identify, assess, manage and mitigate risk and which is subject to continual re-evaluation.

**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. The Asset and Liabilities Committee is responsible for monitoring the arrears profile and treasury counterparty risk whilst the Board approves changes to counterparties, treasury or lending policy.

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.

An aspect of credit risk is **concentration risk**, which in the asset portfolio can arise from product type, geographical concentration and over exposure to single borrowers, investors or counterparties. The Society takes particular note of concentration risk arising from large exposures which results from the relatively small size of the Society. The Board sets limits for maximum exposure to both borrowers and treasury counterparties.

**Liquidity risk** is the risk that the Society will be unable to meet current and future financial commitments as they fall due or can only do so at excessive cost. The Society's Board-approved liquidity policy is to maintain sufficient liquid resources to cover cash flow requirements 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 as they become due. This is managed by investing according to a Board-approved policy and risk appetite. A significant majority of liquidity is invested with the Bank of England and in UK Government Treasury Bills. A limited amount of liquidity is held as short term deposits with approved banks and building society counterparties domiciled and authorised in the UK. The Society's approach to liquidity risk is documented in its Internal Liquidity Assessment Process (ILAAP).

**Interest rate risk** is the risk that income or expenditure arising from the Society's assets or liabilities varies 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 mortgage lending.

**Operational risk** is the risk of loss resulting from inadequate or failed internal processes, systems or human error, failure to comply with regulatory requirements, key supplier failure or external events. The Society mitigates this risk through having a robust and effective internal control framework, including the Society's compliance function and internal audit, which are overseen by the Risk, Audit, Compliance and Ethics Committee.

**Regulatory and legal risk** is the risk that the volume and complexity of regulatory issues may reduce the Society's capital and ability to compete and grow, or result in fines, public censure or restitution costs because of failure to understand, interpret, implement and comply with UK and EU regulatory requirements. In light of the increasing regulatory demands faced by the sector the Board is alive to the potential increase posed by regulatory risk. The Society has an internal compliance function to monitor compliance with existing legislation,

> ***"The Society continues to invest in its technology infrastructure so that it can maintain and develop services that meet the emergent needs and expectations of its members and the financial services market."***

the implementation of controls and the impact of new requirements. This is overseen by the Risk, Audit, Compliance and Ethics Committee.

**Reputational risk** – the unique nature of the Society gives rise to a specific form of reputational risk. The Society must ensure that it is apparent 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.

**Conduct risk** is the risk that the Society fails to treat its customers fairly and delivers poor customer outcomes. The Society considers conduct risk to be a sub-set of wider ethical considerations and therefore maintains an overarching ethics risk framework, which fully addresses all aspects of the Society's interactions with society and the environment while providing assurance that conduct issues are appropriately addressed in the Society's culture.

**Strategic risk** is the current and prospective impact on cash resources; earnings or capital arising from adverse business decisions; improper implementation of business decisions or a lack of responsiveness to changes in the industry or the external environment. They represent all high level risks faced by the Society arising from external factors given the Society's business model and direction.

Strategic risk has arisen as a result of the UK's referendum on leaving the European Union. The full impact of the UK's exit from the EU remains uncertain and there continue to be differing views regarding the effect it will have on the UK economy in the longer term. Potentially this could negatively affect other risks such as credit risk and interest rate risk which have been described above.

## IT and information security

The Society continues to invest in its technology infrastructure so that it can maintain and develop services that meet the emergent needs and expectations of its members and the financial services market in which the Society operates.

*Wind turbine at an Ecology borrower's property*

> *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.*

Whilst there is a strong focus on the development of customer interfaces and services, the Society is also fully cognisant of external threats, in particular cybercrime attacks designed to deny access to systems and compromise or misuse data and assets held on Society systems. The Society has dedicated first and second line security functions with specific responsibilities to protect the Society and members' assets.

Independent exercises are undertaken to test the Society's defences and to ensure that cyber controls evolve in line with the ever-changing threat landscape. A recent independent external security assessment showed the Society to be at the top of the range for financial services institutions due to the controls and behaviours employed.

## Financial risk management objectives and policies

The Society has a formal structure for managing financial risk. This risk is closely monitored and controlled by the Board, supported by the Risk Committee and the Risk, Audit, Compliance and Ethics Committee (RACE). The Assets and Liabilities Committee actively measures and manages financial risks. 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 23.

## Charitable donations

During the year, the Society made charitable donations amounting to £11,765 (2016: £13,350). No contributions were made to political parties.

## Land and buildings

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. The energy generated for the year is around 18.4% (2016: 18.8%) of our needs, with the remainder supplied from off-site renewable sources.

## Supplier payment policy and practice

All suppliers are requested to furnish the Society with a copy of their environmental policy, and the quality of the policies 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 2017 was 44 days (2016: 44 days).

## Tax policy

The Society is committed to paying all the taxes that it owes in accordance with the spirit of all tax laws that apply to its operations. The Society adopted a Tax Compliance Policy Statement on 29 January 2016. A copy is available on our website at **ecology.co.uk/about/corporate**.

In 2015 the Society received the Fair Tax Mark, which confirms that, as a good corporate citizen, it actively welcomes paying its fair share of tax.

The disclosure made in these annual report and accounts comply with commitments made in that policy statement.

## Management and staff

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

> *In 2015 the Society received the Fair Tax Mark, which confirms that, as a good corporate citizen, it actively welcomes paying its fair share of tax.*

A comprehensive programme of staff training and development has continued during the year enabling staff to continue to develop relevant skills and knowledge, ensuring that we maintain an excellent level of service to our members. The Society has a commitment to fair remuneration practices.

The Directors would like to record their appreciation of the loyalty and commitment of management and wider staff team. Their support and contribution in a challenging environment is the backbone of the continuing success of the Society.

## Going concern

The Directors have prepared forecasts of the Society's capital position, financial position and liquidity position for the period ending twelve months from the date of approval of these financial statements. In doing so they have also considered the effect of extreme but plausible events that would impact on the Society's business and have concluded that the Society has adequate resources to continue in business for the foreseeable future. For this reason the accounts continue to be prepared on a going concern basis.

In common with other deposit-taking 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. Accordingly, the accounts continue to be prepared on a going concern basis.

## Auditor

The auditor, KPMG LLP, has expressed its willingness to continue in office and therefore a resolution for their reappointment will be proposed to the forthcoming Annual General Meeting of the Society.

## Directors

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

**Paul Ellis**
Chief Executive

**Andrew Gold**

**Tim Morgan**

**Chris Newman**

**Louise Power**

**Steve Round**
Chair from 25 April 2015

**Vincent Smith**
appointed 3 November 2017

**Alison Vipond**
Deputy Chair

**Pam Waring**
Finance Director and Secretary

Steve Round and Andrew Gold are to retire by rotation and, being eligible, offer themselves for re-election at the AGM.

Vincent Smith was co-opted on to the Board in 2017 and in accordance with the provision of Rule 25(4), is required to stand for election at the AGM. The Board appoints Directors who can offer specific skills and experience to the Society. Vincent has 28 years of corporate treasury management experience working for large companies and, in addition, he is Vice-President of Staffordshire Wildlife Trust, having served as a trustee for 21 years.

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.

## Post balance sheet events

The Board considers that there have been no events since the end of the year that have a material effect on the financial position of the Society.

On behalf of the Board

Steve Round
*Chair*
2 March 2018

# Corporate governance report

## Overview

The Board is responsible for the governance of the Society on behalf of its members. The Board is committed to good practice in corporate governance, and has regard to the principles of the UK Corporate Governance Code (April 2016) issued by the Financial Reporting Council. The Code is addressed to listed companies, but the Board agrees with and supports its general principles and follows those elements that are considered to be appropriate and proportionate to Ecology. In addition the Society adheres to the supervisory approach, 'Strengthening Accountability in UK Banking', a senior manager certification regime which came into effect in March 2016

## The Board

The Board works with management to set the Society's strategic and policy direction, acting in the best interests of its members in respect of both their financial and ethical objectives. 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, 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 Board meets at least nine times a year and by teleconference if there is a business requirement to do so.

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. The schedule of retained and delegated powers is reviewed regularly.

> ***"The Board works with management to set the Society's strategic and policy direction, acting in the best interests of its members."***

## Board composition and independence

All Directors must meet the test of fitness and propriety as laid down by the regulator to fulfil their role as Directors. Because we do not have an equity shareholding model, we do not appoint a senior independent director, as this has little relevance to the small building society model. We have appointed Alison Vipond as the Member Advocacy Director to be the first line of communication for members and the Board. Our model of encouraging participation, particularly through AGMs, provides a better way of ensuring sensitivity to member concerns.

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. By exception, we allow annual election for a Director beyond the nine-year period, to enable us to retain skills for further short periods should we, as a small Society requiring Directors to be drawn from our 'constituency', be unable to readily identify an available candidate currently in regard to a particular skill set. Where a Director who has served nine years is appointed Chair, the election period reverts to three years.

The Society's Rules require that all Directors are submitted for election at the 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.

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 publication of vacancies in the Society newsletter, the Society website, and on social media. 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.

Within prudential constraints, the Board aims at diversity in its membership aiming particularly at gender balance and diversity of age. During 2017, 3 out of 9 of Board members were female. All Board vacancies are communicated via Women on Boards.

## 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 appraise 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. The Board also assesses the effectiveness of its decision-making after each meeting.

An assessment of the Board's performance against predetermined criteria is carried out each year with further comment where appropriate. Each evaluation is scored and the results collated by the Board Governance Officer. The Deputy Chair provides a summary of the results for the Board who note any action on improvements that can be made.

## Risk management, internal control and Board committees

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 responsible for risk identification and day-to-day operation of the risk management framework.

> ***...the Society holds that the conduct of its business must result in tangible environmental and social benefits...***

The Board has overall responsibility for the Society's internal control system and for reporting its effectiveness to the members in the annual financial statements. Senior management has the task of designing, operating and monitoring 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.

The effectiveness of the Society's risk management framework is monitored and reported on by internal audit.

## 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.

The composition and effectiveness of the Committee are reviewed annually by the Board. 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 five times during 2017.

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 Tim Morgan. At the invitation of the Chair of the Committee, the Chief Executive, Finance Director, Chief Risk Officer, Compliance Manager, Risk and Ethics Manager and representatives from both internal and external audit attend meetings.

RACE reviews the Annual Report and Accounts with the external auditors and executive management and, if appropriate, recommends approval of these at the next full Board meeting. After discussion with senior management, the Committee considered and confirmed that the key risks of mis-statement in the Society's financial statements relate to the following judgements:

- provision for loan loss impairment
- revenue recognition
- valuation of non-basic financial instruments

These issues were discussed with the external auditors through the audit process and at the conclusion of the audit process to confirm the financial statements for approval.

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 Risk and Ethics Manager.

The Committee monitors the independence and effectiveness of internal and external audit. At RACE meetings during the year the members have discussed the effectiveness of the external auditors using evidence from regular written reports including KPMG LLP's Statement of Independence presented to RACE in September 2017, and held discussions with the audit director. KPMG have been the Society's auditors for over 20 years but operate an audit partner rotation policy. It was concluded that, while the auditors were carrying out their duties objectively, effectively and independent of management, as the last tender was undertaken in 2005, it is the intention of the Board to conduct a tender process by 2020 at the latest. The Board recommendation at the AGM is to appoint KPMG LLP for another year.

At the RACE meeting in June 2017 a Policy was approved that set out the circumstances where external audit may be used for non audit services.

## Assets and Liabilities Committee (ALCO)

The remit of the Committee is to monitor and control 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 Committee is chaired by the Chief Executive with the other members being the Finance Director, Chief Operating Officer and two Non-Executive Directors. The Committee met six times during 2017.

### 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 currently chaired by Chris Newman. The Committee met three times during 2017.

### Board Lending Committee

The Committee examines credit risks, which include non-standard and non-residential lending proposals. It also reviews potential changes to lending policy and limits. The Committee comprises two Non-Executive Directors, two consultants who have relevant experience of the Society's lending sectors, and is attended by the Chief Executive, the Chief Operating Officer, and other staff members as appropriate. The Committee is chaired by Chris Newman and met four times during 2017.

### Nominations Committee

This Committee is responsible for succession planning and for reviewing applications for the post of Non-Executive Director and making a recommendation to the full Board. The Committee is comprised of one Executive Director and two Non-Executive Directors. The Committee is currently chaired by Steve Round and it met on two occasions in 2017.

The function and details of the **Remuneration Committee** are disclosed within the Directors' Remuneration Report on pages 22-24. The Committee is chaired by Andrew Gold.

## Board and committee membership and attendance record

| Director | Board | Risk, Audit, Compliance and Ethics | DSPC | Board Lending | Remuneration | Nominations | ALCO |
|---|---|---|---|---|---|---|---|
| **Paul Ellis*** | 8/9 | 4/5 | 3/3 | 4/4 | ■ | 2/2 | 6/6 |
| **Andrew Gold*** | 9/9 | 5/5 | 3/3 | ■ | 1/1 | ■ | 6/6 |
| **Tim Morgan** | 8/9 | 5/5 | 3/3 | 4/4 | 1/1 | ■ | ■ |
| **Chris Newman** | 9/9 | 5/5 | 3/3 | 4/4 | ■ | ■ | ■ |
| **Louise Power** | 7/9 | ■ | 3/3 | 4/4 | ■ | 2/2 | ■ |
| **Steve Round** | 9/9 | ■ | 2/3 | ■ | ■ | 2/2 | 5/6 |
| **Alison Vipond** | 9/9 | 5/5 | 3/3 | ■ | 1/1 | 1/1 | ■ |
| **Pam Waring*** | 9/9 | 5/5 | 3/3 | ■ | ■ | ■ | 5/6 |
| **Vincent Smith** | 2/2 | ■ | 1/1 | ■ | ■ | ■ | ■ |

*Directors are invited attendees of RACE

All Non-Executive Directors are actively encouraged to attend committee meetings that they are not a member of as part of their ongoing training.

■ *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 FCA 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 contractual arrangements of the Chair of the Board, the executive directors and executive management. It is also responsible for making recommendations to the Board on the level of remuneration for Non-Executive Directors. In addition, it reviews general salary levels.

The Committee is comprised of three Non-Executive Directors. The Chief Executive and Finance Director attend by invitation. The Chief Executive and Finance Director take no part in the discussion concerning their individual remuneration. The Committee held one meeting during 2017 at which all members of the Committee were in attendance. The Committee reviews supporting evidence, including external professional advice if appropriate, on comparative remuneration packages.

> ***The Society has a long-established fair pay policy which limits the ratio between the highest and the lowest basic salary.***

## Remuneration policy

### Non-Executive Directors

Non-Executive Directors receive a fee for their services that reflects the time commitment for their duties. There are no performance related pay schemes for Non-Executive Directors and they do not qualify for pension or other benefits.

Non-Executive Directors do not have service contracts but serve under letters of appointment. The contribution of each Non-Executive Director is appraised by the Chair annually.

### Executive Directors

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

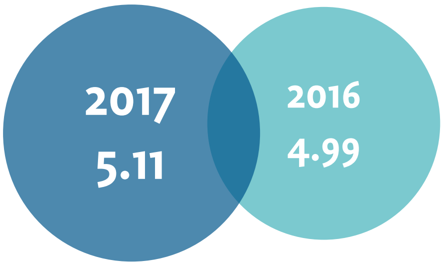
All fees earned by Executive Directors serving on external boards are paid to the Society.

### 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 Society is committed to paying the Living Wage and has received accreditation for this from the Living Wage Foundation.

The Society has a long-established fair pay policy which limits the ratio between the highest and the lowest basic salary. Following consultation with the Society's Ethics Panel this was increased to a multiple of eight times the lowest full grade with effect from January 2017. The Society continues to monitor good practice in remuneration disclosures and, as such, is awaiting the outcome of the Government's deliberations on potential legislation to support the revised UK Corporate Governance Code recommendation of disclosing the ratio of the CEO's pay to the average pay of all employees.

## Ratio of highest basic salary to lowest full grade available




### Performance related pay

This is an annual scheme that provides non-pensionable rewards directly linked to the achievement of key performance objectives aimed at personal and professional development. The overall objective is to improve Society performance whilst maintaining the financial strength of the Society for the long term benefit of its members.

### Pensions

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.

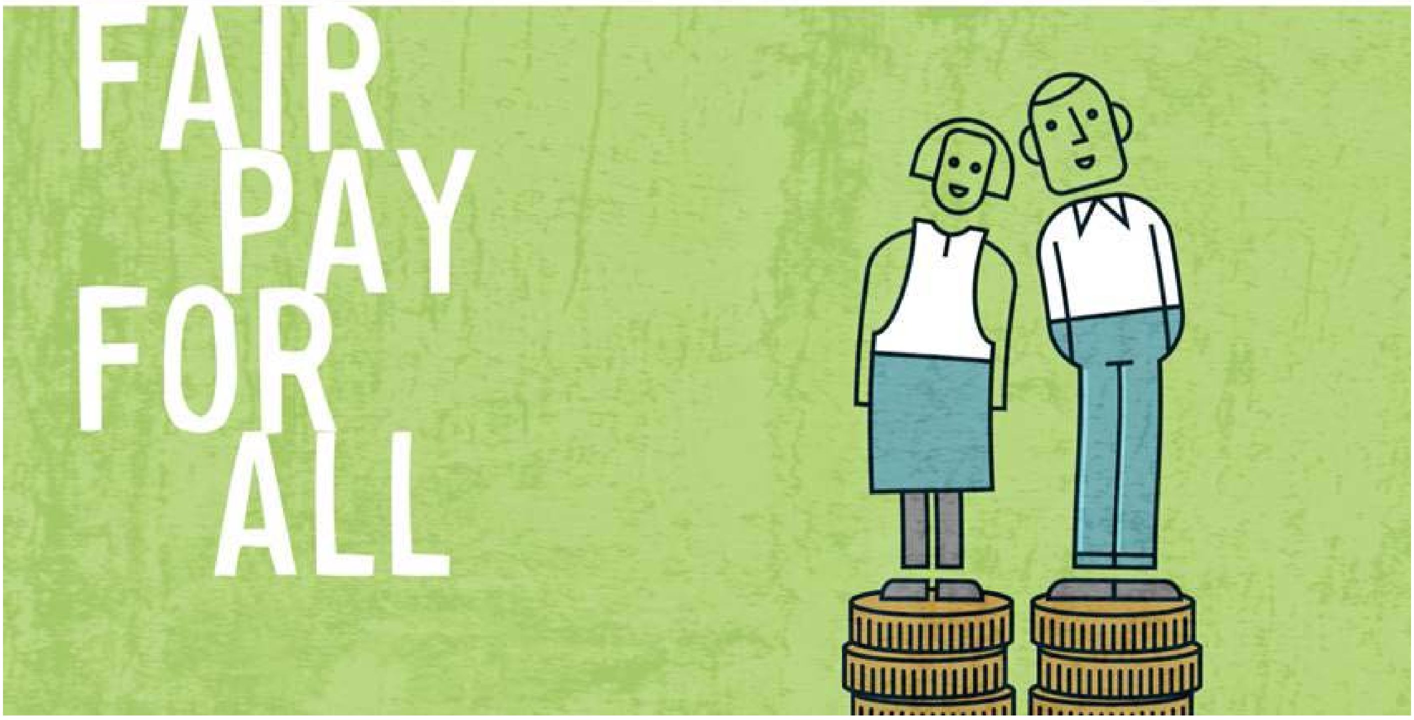
### Benefits

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.

### 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, Finance Director, has a service contract entered into on 28 December 2001. Both contracts are terminable by either party giving six months' notice.

***The Society is committed to paying the Living Wage and has received accreditation for this from the Living Wage Foundation.***



## Non-Executive Directors' remuneration

| | 2017 £000 | 2016 £000 |
|---|---|---|
| **Andrew Gold**[1] | **22** | 19 |
| **Tim Morgan** | **14** | 11 |
| **Chris Newman** | **14** | 11 |
| **Steve Round** | **17** | 16 |
| **Vincent Smith** (appointed 3 November 2017) | **2** | – |
| **Alison Vipond** | **12** | 12 |
| **Totals** | **81** | 69 |

[1] *Includes additional remuneration of £10,461 (2016: £9,117) in relation to assigned senior management regime responsibilities for oversight of the risk function.*

Under the terms of her employment Louise Power, a partner at Walker Morris LLP, is unable to be remunerated directly by the Society. Walker Morris LLP is paid for her service as a Non-Executive as noted below:

| | 2017 £000 | 2016 £000 |
|---|---|---|
| **Louise Power** | **12** | 8 |
| **Totals** | **12** | 8 |

## Executive Directors' remuneration

| | Salary £000 | Performance related pay £000 | Taxable benefits* £000 | Contributions to pension scheme £000 | Total £000 |
|---|---|---|---|---|---|
| **2017** | | | | | |
| **Paul Ellis (Chief Executive)** | **84** | **4** | **2** | **7** | **97** |
| **Pam Waring (Finance Director)** | **73** | **4** | **–** | **6** | **83** |
| **Totals** | **157** | **8** | **2** | **13** | **180** |
| 2016 | | | | | |
| Paul Ellis (Chief Executive) | 81 | 7 | 2 | 6 | 96 |
| Pam Waring (Finance Director) | 70 | 5 | – | 6 | 81 |
| **Totals** | **151** | **12** | **2** | **12** | **177** |

On behalf of the Board
**Steve Round**
*Chair*
2 March 2018

# Statement of Directors’ responsibilities

## Statement of Directors’ responsibilities in respect of the annual report, the annual business statement, the Directors’ report and annual accounts

The Directors are responsible for preparing the Annual Report, Annual Business Statement, Directors’ Report and the annual accounts in accordance with applicable law and regulations.

The Building Societies Act 1986 (“the Act”) requires the Directors to prepare the Society’s annual accounts for each financial year. Under that law they have elected to prepare the Society’s annual accounts in accordance with UK accounting standards and applicable law (UK Generally Accepted Accounting Practice) including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland.

The Society’s 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 the 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 containing 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 group and 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 Conduct Authority and Prudential Regulation 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.

**Steve Round**
*Chair*
2 March 2018

# Independent auditor's report to the members of Ecology Building Society

## 1. Our opinion is unmodified

We have audited the annual accounts of Ecology Building Society for the year ended 31 December 2017, comprising of: statement of comprehensive income, statement of changes in members' interests, statement of financial position, cash flow statement, and the related notes, including the accounting policies in note 1.

### In our opinion the annual accounts:

- give a true and fair view of the state of affairs of the Society as at 31 December 2017 and of the income and expenditure of the Society for the year then ended;
- have been properly prepared in accordance with UK accounting standards, including FRS 102 The Financial Reporting Standard applicable in the UK and Republic of Ireland; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and regulations made under it.

### Basis for opinion:

We conducted our audit in accordance with International Standards on Auditing (UK) ("ISAs (UK)") and applicable law. Our responsibilities are described below. We believe that the audit evidence we have obtained is a sufficient and appropriate basis for our opinion. Our audit opinion is consistent with our report to the Risk, Audit, Compliance and Ethics Committee (RACE). We were appointed as auditor by the members in 1994. The period of total uninterrupted engagement is for the 23 financial years ended 31 December 2017.

We have fulfilled our ethical responsibilities under, and we remain independent of the Society in accordance with, UK ethical requirements including the FRC Ethical Standard applicable to public interest entities. No non-audit services prohibited by that standard were provided.

**Overview**

| | | |
|---|---|---|
| **Materiality:** financial statements as a whole | | £50,000 (2016: £89,000) 5.0% (2016: 8.0%) of profit before tax from continuing operations |
| **Coverage** | | 5.0% (2016: 8.0%) of profit before tax |
| **Risks of material misstatement** | | **vs 2016** |
| **Recurring risks** | Impairment of loans | ↔ |
| | Valuation of non-basic financial instruments | ↑ |
| | Effective interest rate income recognition | ↔ |

## 2. Key audit matters: our assessment of risks of material misstatement

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the financial statements and include the most significant assessed risks of material misstatement (whether or not due to fraud) identified by us, including those which had the greatest effect on: the overall audit strategy; the allocation of resources in the audit; and directing the efforts of the engagement team. We summarise below the key audit matters, in decreasing order of audit significance, in arriving at our audit opinion above, together with our key audit procedures to address those matters and, as required for public interest entities, our results from those procedures. These matters were addressed and our results are based on procedures undertaken, in the context of, and solely for the purpose of, our audit of the financial statements as a whole, and in forming our opinion thereon, and consequently are incidental to that opinion, and we do not provide a separate opinion on these matters.

| | The risk | Our response |
|---|---|---|
| **Impairment of loans**<br><br>*(Impairment provision £624,000 (2016: £662,000)*<br><br>*Refer to page 20 (RACE Report), page 36 (accounting policy) and page 52 (financial disclosures).* | **Subjective estimate:**<br><br>Impairments cover loans specifically identified as impaired and a collective impairment of all other loans for those impairments incurred but not yet specifically identified.<br><br>Individual impairments are considered on loans that are in arrears by one or more months or forborne without a payment shortfall with LTV greater than 50% (70% for large exposures); as well as commercial cases on review that have financial/governance issues. There is a risk an impaired loan has not been provided for based on the discount applied to the security.<br><br>The collective impairment is derived from a model that uses a combination of the Society's historical experience and, due to the Society's limited loss experience, the professional judgement of the directors. In particular, judgement is required on the time to sale and forced sale discounts against collateral, which the provision is sensitive to. Loans that have been individually considered are excluded from the collective population. | Our procedures included:<br><br>**Benchmarking assumptions:** We compared the key assumptions used in the model for forced sale discounts and 'time from default to sale' applied with externally available data, including KPMG's building society database. We compared the loan portfolio key metrics, including arrears trends and provision coverage with those of comparable lenders.<br><br>**Our sector experience:** We challenged the key impairment assumptions used in the model for forced sale discounts and time to sale using our knowledge of recent impairment experience in this industry.<br><br>**Sensitivity analysis:** We assessed the collective model and specific individual impairments for their sensitivities to changes in the key assumptions, by performing stress testing to help us assess the reasonableness of the assumptions and identify areas of potential additional focus.<br><br>**Assessing transparency:** We assessed the adequacy of the Society's disclosures about the degree of estimation involved in arriving at the provision.<br><br>**Our results**<br><br>We found the resulting estimate of the impairment provision to be acceptable (2016: acceptable). |

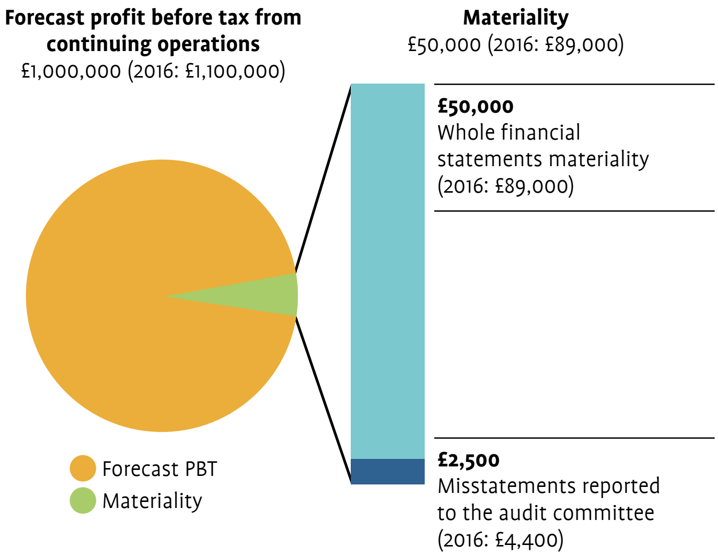
| | The risk | Our response |
|---|---|---|
| **Valuation of non-basic financial instruments**<br><br>*(Asset valuation £539,000 (2016: £61,000)*<br><br>*Refer to page 20 (RACE Report), page 36 (accounting policy) and page 37 (financial disclosures).* | **Subjective estimate:**<br><br>The Society holds a number of fixed asset investments that are considered 'non basic' under FRS102. These are required to be held at fair value. A number of these investments are either not traded on an active market, or are traded on a limited market at significantly lower values than the Society's investment. In these cases the Society is at risk of becoming the 'price setter' were it to quickly dispose of its investments.<br><br>Due to the judgement involved by the directors determining the investments' value in the absence of a market price, there is estimation uncertainty with regard to the fixed asset investment measured at fair value. | Our procedures included:<br><br>**Methodology choice:** In the context of observed industry best practice, we challenged the appropriateness of the valuation basis selected.<br><br>**Our valuations experience:** Challenging management on key judgements affecting the investee company valuations, such as the relevance of recent market activity, where it can be observed. We compared key underlying financial data inputs to external sources. In certain cases we have engaged valuations specialists to provide an alternative valuation using observable market data.<br><br>**Comparing valuations:** Where a recent transaction has been used to value a holding, we obtained an understanding of the circumstances surrounding the transaction and its relevance to the Society's investments; and therefore we considered its suitability as an input into the valuations used by the Society.<br><br>**Assessing transparency:** We considered the appropriateness, in accordance with relevant accounting standards, of the disclosures in respect of non-basic investments and the effect of changing one or more inputs to reasonably possible alternative valuation assumptions.<br><br>**Our results**<br><br>We found the valuation of the non-basic investments to be acceptable (2016: Not considered a key audit matter, but found to be acceptable). |

| | The risk | Our response |
|---|---|---|
| **Effective interest rate income recognition**<br><br>*(EIR income £54,884 (2016: £34,753; year end EIR asset £128,500 (2016: £140,952))*<br><br>*Refer to page 20 (RACE Report), page 20 (accounting policy) and page 42 (financial disclosures).* | Subjective estimate:<br><br>Using an Excel model, fees earned on loans are recognised using the effective interest rate ('EIR') method that spreads directly attributable cash flows over the expected lives of the loans.<br><br>The directors apply judgement in deciding and assessing the expected repayment profiles used to determine the EIR. The most critical element of judgement in this area is the estimation of the future redemption profiles of the loans. This is informed by product mix and past customer behaviour of when loans are repaid. | Our procedures included:<br><br>**Our sector experience:** We assessed the key assumptions behind the expected customer lives and profiles of significant loan products against our own knowledge of industry experience and trends, including benchmarking with comparable lenders.<br><br>**Sensitivity analysis:** We assessed the models for their sensitivities to changes in the key assumptions by considering different profiles to help us assess the reasonableness of the assumptions used and identify areas of potential additional focus.<br><br>**Historical comparison:** We assessed the reasonableness of the model's expected repayment profile assumptions against historical experience of loan lives, based on customer behaviour, product mix and recent performance.<br><br>**Assessing transparency:** We assessed the adequacy of the Society's disclosures about the degree of estimation involved in arriving at the interest income recognised.<br><br>**Our results**<br><br>We found the resulting estimate of the EIR to be acceptable (2016: acceptable) |

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

Materiality for the financial statements as a whole was set at £50,000 (2016: £89,000), determined with reference to a benchmark of profit before tax from continuing operations (of which it represents 5.0% (2016: 8.0%)).

We agreed to report to the Audit Committee any corrected or uncorrected identified misstatements exceeding £2,500 (2016: £4,400), in addition to other identified misstatements that warranted reporting on qualitative grounds.



## 4. We have nothing to report on going concern

We are required to report to you, if we have concluded that the use of the going concern basis of accounting is inappropriate, or there is an undisclosed material uncertainty that may cast significant doubt over the use of that basis, for a period of at least twelve months from the date of approval of the financial statements. We have nothing to report in these respects.

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

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

Our responsibility is to read the other information and, in doing so, consider whether, based on our financial statements audit work, the information therein is materially misstated or inconsistent with the financial statements or our audit knowledge. Based solely on that work we have not identified material misstatements in the other information.

### *Annual Business Statement and Directors' Report*

### 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 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.

## 6. We have nothing to report on the other matters on which we are required to report by exception

Under the Building Societies Act 1986 we are required to report to you if, in our opinion:

- adequate accounting records have not been kept by the Society; or
- the financial statements [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.

We have nothing to report in these respects.

## 7. Respective responsibilities

### Directors' responsibilities

As explained more fully in their statement set out on page 25, the directors are responsible for: the preparation of annual accounts which give a true and fair view; such internal control as they determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error; assessing the Society's ability to continue as a going concern, disclosing, as applicable, matters related to going concern; and using the going concern basis of accounting unless they either intend to liquidate the Society or to cease operations, or have no realistic alternative but to do so.

## Auditor's responsibilities

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud, other irregularities, or error, and to issue our opinion in an auditor's report. Reasonable assurance is a high level of assurance, but does not guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements. The risk of not detecting a material misstatement resulting from fraud or other irregularities is higher than for one resulting from error, as they may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control and may involve any area of law and regulation not just those directly affecting the financial statements.

A fuller description of our responsibilities is provided on the FRC's website at **frc.org.uk/auditorsresponsibilities**.

### *Irregularities – ability to detect*

Our audit aimed to detect non-compliance with relevant laws and regulations (irregularities) that could have a material effect on the annual report and accounts. We identified relevant areas of laws and regulations from our sector experience, through discussion with the directors (as required by auditing standards), and from inspection of the society's regulatory and legal correspondence.

We had regard to laws and regulations in areas that directly affect the financial statements including financial reporting (including related building society legislation) and taxation legislation. We considered the extent of compliance with those laws and regulations as part of our procedures on the related annual report and accounts items.

In addition we considered the impact of laws and regulations in the specific areas of regulatory capital and liquidity, conduct including PPI mis-selling, money laundering, sanctions list and financial crime, and certain aspects of company legislation recognising the financial and regulated nature of the society's activities and its legal form. With the exception of any known or possible non-compliance, and as required by auditing standards, our work in respect of these was limited to enquiry of the directors and inspection of regulatory and legal correspondence. We considered the effect of any known or possible non-compliance in these areas as part of our procedures on the related annual report and accounts items.

We communicated identified laws and regulations throughout our team and remained alert to any indications of non-compliance throughout the audit

## 8. The purpose of our audit work and to whom we owe our responsibilities

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.

**David Allen** (Senior Statutory Auditor)
**for and on behalf of KPMG LLP, Statutory Auditor**
*Chartered Accountants*

1 Sovereign Square
Sovereign Street
Leeds
LS1 4DA

2 March 2018

# Statement of comprehensive income

*for the year ended 31 December 2017*

| | Notes | **2017 £000** | 2016 £000 |
|---|---|---|---|
| Interest receivable and similar income | 2 | **5,473** | 5,828 |
| Interest payable and similar charges | 3 | **(1,876)** | (2,086) |
| **Net interest income** | | **3,597** | 3,742 |
| Income from investments | | **45** | 26 |
| Fees and commissions receivable | | **8** | 8 |
| Fees and commissions payable | | **(41)** | (44) |
| Other operating income | | **30** | 18 |
| Net loss from other financial instruments at fair value through profit and loss | | **(8)** | 2 |
| **Total net income** | | **3,631** | 3,752 |
| Administrative expenses | 4 | **(2,378)** | (2,217) |
| Depreciation and amortisation | 13,15 | **(121)** | (89) |
| **Operating profit before impairment losses and provisions** | | **1,132** | 1,446 |
| Impairment losses on loans and advances | 12 | **20** | (260) |
| Provisions for liabilities | 21 | **(40)** | (68) |
| **Profit before tax** | | **1,112** | 1,118 |
| Tax expense | 7 | **(197)** | (198) |
| **Profit for the financial year** | | **915** | 920 |
| Other comprehensive income | | **–** | – |
| **Total comprehensive income for the year** | | **915** | 920 |

Profit for the financial year arises from continuing operations. The profit for the financial year is attributable to the members of the Society.

Further comments on the income and expenditure account line items are presented in the notes to the financial statements.

# Statement of financial position

*at 31 December 2017*

| Assets | Notes | 2017 £000 | 2016 £000 |
|---|---|---|---|
| Liquid assets | | | |
| Cash in hand and with the Bank of England | 8 | **41,614** | 36,192 |
| Treasury bills and similar securities | 10 | **3,998** | 8,496 |
| Loans and advances to credit institutions | 9 | **11,494** | 7,115 |
| Debt securities | 10 | **3,520** | – |
| Loans and advances to customers | 11 | **114,412** | 117,989 |
| Tangible fixed assets | 13 | **1,225** | 1,294 |
| Investments | 14 | **2,060** | 1,609 |
| Intangible assets | 15 | **68** | 103 |
| Other debtors | 16 | **271** | 258 |
| **Total assets** | | **178,662** | 173,056 |
| **Liabilities** | | | |
| Shares | 17 | **157,603** | 153,701 |
| Amounts owed to other customers | 18 | **10,171** | 9,375 |
| Subordinated liabilities | 22 | **749** | 749 |
| Other liabilities | 19 | **360** | 336 |
| Accruals | | **137** | 110 |
| Deferred tax liability | 20 | **29** | 37 |
| Other provisions | 21 | **18** | 68 |
| **Total liabilities** | | **169,067** | 164,376 |
| Reserves | | | |
| General reserves | | **9,595** | 8,680 |
| | | | |
| Total reserves attributable to members of the Society | | **9,595** | 8,680 |
| **Total reserves and liabilities** | | **178,662** | 173,056 |

These accounts were approved by the Board of Directors on 2 March 2018 and were signed on its behalf by:

**Steve Round**
*Chair*

**Paul Ellis**
*Chief Executive*

**Pam Waring**
*Finance Director*

# Statement of changes in members' interests

| | **General reserve 2017 £000** | **Total 2017 £000** | General reserve 2016 £000 | Total 2016 £000 |
|---|---|---|---|---|
| Balance at 1 January | **8,680** | **8,680** | 7,760 | 7,760 |
| **Total comprehensive income for the period** | | | | |
| Profit for the year | **915** | **915** | 920 | 920 |
| Other comprehensive income | **–** | **–** | – | – |
| Total comprehensive income for the period | **915** | **915** | 920 | 920 |
| **Balance at 31 December** | **9,595** | **9,595** | 8,680 | 8,680 |

# Cash flow statement

| Cash flows from operating activities | Notes | 2017 £000 | 2016 £000 |
|---|---|---|---|
| Profit before tax | | **1,112** | 1,118 |
| Adjustments for | | | |
| Depreciation and amortisation | 13,15 | **121** | 89 |
| Impairment of investment | 14 | **8** | (2) |
| Interest on subscribed capital | 3 | **23** | 57 |
| Provision for liabilities | | **40** | 68 |
| Loans and advances written off in the year | 12 | **18** | – |
| Increase in impairment of loans and advances | 12 | **(38)** | 260 |
| **Total** | | **1,284** | 1,590 |
| **Changes in operating assets and liabilities** | | | |
| Increase in prepayments, accrued income and other assets | | **(13)** | (22) |
| Increase in accruals, deferred income and other liabilities | | **28** | 5 |
| Decrease/(increase) in loans and advances to customers | | **3,597** | (4,737) |
| (Increase)/decrease in loans and advances to credit institutions | | **(2,006)** | 502 |
| Increase in shares | | **3,902** | 26,268 |
| Increase in amounts owed to other credit institutions and other customers | | **796** | 563 |
| Decrease in amounts owed – Subordinated liabilities | | **–** | (499) |
| Decrease in other liabilities | | **(4)** | (148) |
| FSCS interest cost paid | | **(24)** | (40) |
| Other provision paid | | **(66)** | – |
| Taxation paid | | **(178)** | (208) |
| **Net cash generated by operating activities** | | **7,316** | 23,274 |
| **Cash flows from investing activities** | | | |
| Purchase of debt securities | 10 | **(6,552)** | – |
| Disposal of debt securities | 10 | **3,033** | – |
| Purchase of treasury bills | 10 | **(5,532)** | (17,003) |
| Disposal of treasury bills | 10 | **10,030** | 14,000 |
| Purchase of investments | 14 | **(490)** | (486) |
| Repayment of investments | 14 | **31** | – |
| Purchase of tangible fixed assets | 13 | **(17)** | (88) |
| Purchase of intangible assets | 15 | **–** | (82) |
| **Net cash generated by/(used in) investing activities** | | **503** | (3,659) |
| **Cash flows from financing activities** | | | |
| Interest paid on subscribed capital | 3 | **(23)** | (57) |
| **Net increase/(decrease) in cash and cash equivalents** | | **7,796** | 19,558 |
| Cash and cash equivalents at 01 January | | **42,305** | 22,747 |
| **Cash and cash equivalents at 31 December** | 8 | **50,101** | 42,305 |

# Notes

*(forming part of the Annual Accounts)*

## 1. Accounting policies

Ecology Building Society (the "Society") has prepared these annual accounts on a going concern basis as outlined in the Director's Report on pages 9 to 13 and in accordance with the Building Societies Act 1986, the Building Societies (Accounts and Related Provisions) Regulations 1998 and Financial Reporting Standard 102, The Financial Reporting Standard, applicable in the UK and Republic of Ireland ("FRS 102") as issued in August 2014. The presentation currency of these annual accounts is sterling. All amounts in the annual accounts have been rounded to the nearest £1,000.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these annual accounts.

In common with other deposit-taking 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. Accordingly, the accounts continue to be prepared on a going concern basis.

### 1.1. Measurement convention

The annual accounts are prepared on the historical cost basis except in the case of Financial Instruments which are measured in line with FRS 102 and treated as either basic or non-basic. Basic instruments are measured at amortised cost and non-basic instruments are stated at their fair value. As per Note 14 certain non-basic financial instruments are carried at amortised cost less impairment, due to the absence of suitable inputs to fair value methodology.

### 1.2. Interest

Interest income and expense are recognised in profit or loss using the amortised cost effective interest method. The 'effective interest rate' (EIR) is the rate that exactly discounts the estimated future cash payments and receipts through the expected life of the financial asset or financial liability (or, where appropriate, a shorter period) to the carrying amount of the financial asset or financial liability.

The calculation of the effective interest rate includes transaction costs and fees and commissions paid or received that are an integral part of the effective interest rate. Transaction costs include incremental costs that are directly attributable to the acquisition or issue of a financial asset or financial liability.

Interest income and expense presented in the income statement and other comprehensive income include interest on financial assets and financial liabilities measured at amortised cost calculated on an effective interest basis.

### 1.3. Fees and commission

Fees and commission income and expense that are integral to the effective interest rate on a financial asset or financial liability are included in the measurement of the effective interest rate (see 1.2).

Other fees and commission income – including account servicing fees and introducers commission on house insurance – is recognised as the related services are performed. If a loan commitment is not expected to result in the draw-down of a loan, then the related loan commitment fees are recognised on a straight-line basis over the commitment period.

Other fees and commission expense relates mainly to introducer fees specific to the Society's revenue generating activities (excluding EIR already covered by 1.2).

### 1.4. Taxation

Tax on the profit or loss for the year comprises current and deferred tax. Tax is recognised in the profit and loss account except to the extent that it relates to items recognised directly in equity or other comprehensive income, in which case it is recognised directly in equity or other comprehensive income.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the balance sheet date, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided on timing differences which arise from the inclusion of income and expenses in tax assessments in periods different from those in which they are recognised in the annual accounts. The following timing differences are not provided for: differences between accumulated depreciation and tax allowances for the cost of a fixed asset if and when all conditions for retaining the tax allowances have been met; and differences relating to investments in subsidiaries, to the extent that it is not probable that they will reverse in the foreseeable future and the reporting entity is able to control the reversal of the timing difference. Deferred tax is not recognised on permanent differences arising because certain types of income or expense are non-taxable or are disallowable for tax or because certain tax charges or allowances are greater or smaller than the corresponding income or expense.

Deferred tax is provided in respect of the additional tax that will be paid or avoided on differences between the amount at which an asset (other than goodwill) or liability is recognised in a business combination and the corresponding amount that can be deducted or assessed for tax.

Deferred tax is measured at the tax rate that is expected to apply to the reversal of the related difference, using tax rates enacted or substantively enacted at the balance sheet date. Deferred tax balances are not discounted.

Unrelieved tax losses and other deferred tax assets are recognised only to the extent that it is probable that they will be recovered against the reversal of deferred tax liabilities or other future taxable profits.

## 1.5. Financial instruments

### Recognition

The Society initially recognises loans and advances, deposits, and subordinated liabilities on the date on which they are originated. All other financial instruments are recognised on the trade date, which is the date on which the Society becomes a party to the contractual provisions of the instrument.

A financial asset or financial liability is measured initially at fair value plus, for an item not at fair value through profit or loss, transaction costs that are directly attributable to its acquisition or issue.

*Financial assets/liabilities*

The Society classifies its financial assets and liabilities into one of the following FRS 102 categories:

- *Basic*

Basic Financial Instruments are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and that the Society does not intend to sell immediately or in the near term. This includes all loans and advances and certain investment as detailed in Note 14.

Basic Financial Instruments are initially measured at fair value plus incremental direct transaction costs, and subsequently measured at their amortised cost using the effective interest method.

The 'amortised cost' of a financial asset or financial liability is the amount at which the financial asset or financial liability is measured at initial recognition, minus principal repayments, plus or minus the cumulative amortisation using the effective interest method of any difference between the initial amount recognised and the maturity amount, minus any reduction for impairment.

Interest income is recognised in profit or loss using the effective interest method (see 1.2). Dividend income is recognised in profit or loss when the Society becomes entitled to the dividend. Impairment losses are recognised in profit or loss.

- *Non Basic*

The Society designates certain Fixed Asset Investments as non-basic financial instruments. Non Basic instruments are financial assets or liabilities that do not meet the definition of a Basic Financial Instrument as per FRS 102 section 11.8 to 11.9. Non Basic Financial Instruments are measured at fair value, with fair value changes recognised immediately in profit or loss. We consider amortised cost to be the equivalent to carrying value where the Instrument is carried at amortised cost less impairment, due to the absence of suitable inputs to fair value methodology. Note 14 details the treatment of each Fixed Asset Investment.

## Fair value measurement

'Fair value' is the amount for which an asset could be exchanged, a liability settled, or an equity instrument granted could be exchanged, between knowledgeable, willing parties in an arm's length transaction.

When available, the Society measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions for the asset or liability take place with sufficient frequency and volume to provide pricing information on an ongoing basis.

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

The best evidence of the fair value of a financial instrument at initial recognition is normally the transaction price – i.e. the fair value of the consideration given or received. If the Society determines that the fair value at initial recognition differs from the transaction price and the fair value is evidenced neither by a quoted price in an active market for an identical asset or liability nor based on a valuation technique that uses only data from observable markets, then the financial instrument is initially measured at fair value, adjusted to defer the difference between the fair value at initial recognition and the transaction price. Subsequently, that difference is recognised in profit or loss on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

## Derecognition

The Society derecognises a financial asset when the contractual rights to the cash flows from the financial asset expire, or it transfers the rights to receive the contractual cash flows in a transaction in which substantially all of the risks and rewards of ownership of the financial asset are transferred or in which the Society neither transfers nor retains substantially all of the risks and rewards of ownership and it does not retain control of the financial asset.

On derecognition of a financial asset, the difference between the carrying amount of the asset (or the carrying amount allocated to the portion of the asset derecognised) and the sum of (i) the consideration received (including any new asset obtained less any new liability assumed) and (ii) any cumulative gain or loss that had been recognised in Other comprehensive income (OCI) is recognised in profit or loss. Any interest in transferred financial assets that qualify for derecognition that is created or retained by the Society is recognised as a separate asset or liability.

The Society derecognises a financial liability when its contractual obligations are discharged or cancelled, or expire.

During the year ending 31 December 2017 the Society has not transferred any financial assets to another party that did not qualify for derecognition.

## Identification and measurement of impairment

At each reporting date, the Society assesses whether there is objective evidence that financial assets not carried at fair value through profit or loss are impaired. A financial asset or a group of financial assets is 'impaired' when objective evidence demonstrates that a loss event has occurred after the initial recognition of the asset(s) and that the loss event has an impact on the future cash flows of the asset(s) that can be estimated reliably.

Objective evidence that financial assets are impaired includes:

- significant financial difficulty of the borrower or issuer
- default or delinquency by a borrower
- the restructuring of a loan or advance by the Society on terms that the Society would not consider otherwise
- indications that a borrower or issuer will enter bankruptcy
- the disappearance of an active market for a security
- observable data relating to a group of assets such as adverse changes in the payment status of borrowers

The Society considers evidence of impairment for loans and advances at both a specific asset and a collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances that are not individually significant are collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

In assessing collective impairment, the Society uses statistical modelling of historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions are such that the actual losses are likely to be greater or lesser than is suggested by historical trends. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Impairment losses on assets measured at amortised cost are calculated as the difference between the carrying amount and the present value of estimated future cash flows discounted at the asset's original effective interest rate.

If the terms of a financial asset are renegotiated or modified or an existing financial asset is replaced with a new one due to financial difficulties of the borrower, then an assessment is made of whether the financial asset should be derecognised. If the cash flows of the renegotiated asset are substantially different, then the contractual rights to cash flows from the original financial asset are deemed to have expired. In this case, the original financial asset is derecognised and the new financial asset is recognised at fair value. The impairment loss before an expected restructuring is measured as follows.

- If the expected restructuring will not result in derecognition of the existing asset, then the estimated cash flows arising from the modified financial asset are included in the measurement of the existing asset based on their expected timing and amounts discounted at the original effective interest rate of the existing financial asset

- If the expected restructuring will result in derecognition of the existing asset, then the expected fair value of the new asset is treated as the final cash flow from the existing financial asset at the time of its derecognition. This amount is discounted from the expected date of derecognition to the reporting date using the original effective interest rate of the existing financial asset

A range of forbearance options are available to support customers who are in financial difficulty. The purpose of forbearance is to support borrowers who have temporary financial difficulties and help them get back on track. The main options offered by the Society include:

- Interest only payments

- Payment holiday

Borrowers requesting a forbearance option will need to provide information to support the request. If the forbearance request is granted the account is monitored in accordance with our policy and procedures. At the appropriate time the forbearance option that has been implemented is cancelled, with the exception of capitalisation of arrears, and the customer's normal contractual payment is restored.

Loans that are subject to restructuring may only be classified as restructured and up-to-date once a specified number and/or amount of qualifying payments have been received. These qualifying payments are set at a level appropriate to the nature of the loan and the customer's ability to make the repayment going forward. Typically the receipt of 6 months of qualifying payments is required.

Impairment losses are recognised in profit or loss and reflected in an allowance account against loans and receivables.

Interest on the impaired assets continues to accrue. If an event occurring after the impairment was recognised causes the amount of impairment loss to decrease, then the decrease in impairment loss is reversed through profit or loss.

## 1.6. Cash and cash equivalents

For the purposes of the Statements of Cash Flows, cash and cash equivalents comprises cash in hand and unrestricted loans and advances to credit institutions. Cash equivalents comprise highly liquid unrestricted investments that are readily convertible into cash with an insignificant risk of changes in value with original maturities of less than three months.

The Statements of Cash Flows have been prepared using the indirect method.

## 1.7. Tangible fixed assets

Tangible fixed assets are stated at cost less accumulated depreciation and accumulated impairment losses.

Where parts of an item of tangible fixed assets have different useful lives, they are accounted for as separate items of tangible fixed assets, for example land is treated separately from buildings.

The Society assesses at each reporting date whether tangible fixed assets are impaired.

Depreciation is charged to the profit and loss account on a straight-line basis over the estimated useful lives of each part of an item of tangible fixed assets. Land is not depreciated. The estimated useful lives are as follows:

- buildings – 50 years
- plant and equipment – 10 years
- fixtures and fittings – 4 to 10 years
- motor vehicles – 4 years
- computer, hardware and associated software – 3 to 5 years

Depreciation methods, useful lives and residual values are reviewed if there is an indication of a significant change since the last annual reporting date in the pattern by which the Society expects to consume an asset's future economic benefits.

## 1.8. Intangible assets

Amortisation is charged to the profit or loss on a straight-line basis over the estimated useful lives of intangible assets. Intangible assets are amortised from the date they are available for use.

The only intangible assets of the Society are software assets for which the useful life is set to 3 to 5 years on the basis of the license or renewal policy.

The Society reviews the amortisation period and method when events and circumstances indicate that the useful life may have changed since the last reporting date.

Intangible assets are tested for impairment in accordance with Section 27 of FRS 102 Impairment of Assets when there is an indication that an intangible asset may be impaired.

## 1.9. Provisions

A provision is recognised in the balance sheet when the Society has a present legal or constructive obligation as a result of a past event, that can be reliably measured and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are recognised at the best estimate of the amount required to settle the obligation at the reporting date.

## 1.10. Assumptions and estimation uncertainties

Certain asset and liability amounts reported in the accounts are based on management estimates, judgements and assumptions. There is, therefore, a risk of changes to the carrying amounts for these assets and liabilities within the next financial year.

**Impairment losses on loans and advances to customers**

To assess impairment, the Society reviews its loan book at least twice yearly. In undertaking this assessment, the Society makes judgments on whether there is evidence that could indicate a material decrease in future cash flows arising from a particular loan portfolio. Estimates are applied on the basis of historical arrears and loss experience for assets with similar credit risk characteristics and objective evidence of impairment. The Society's management also assesses the expected loss on loans and advances as a result of the potential movement in house prices and the likely discount on the sale of properties in possession, based on an understanding of the length of time to disposal. Therefore, the accuracy of provisions made will be affected by changes in these assumptions.

**Effective interest rate (EIR)**

The effective interest rate applied to the mortgage book affects the carrying value of those assets. One of the key components of the Effective Interest Rate is the expected mortgage life. In determining the expected life of mortgage assets, the Society uses historical redemption data as well as management judgement. The expected life of mortgage assets is assessed for reasonableness at least annually.

**Financial instruments and deferred tax assets**

Information about other assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment in the year ending 31 December 2017 are set out in the following notes:

- Note 14 – determination of the fair value of financial instruments with significant unobservable inputs

- Note 20 – recognition of deferred tax assets: availability of future taxable profit against which carry-forward tax losses can be used

## 2. Interest receivable and similar income

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| On loans fully secured on residential property | **4,808** | 5,183 |
| On other loans | **472** | 467 |
| On debt securities | **17** | – |
| On treasury bills at fixed rate interest | **14** | 37 |
| On other liquid assets | **159** | 139 |
| Profit on sale of liquid assets | **1** | – |
| Other interest receivable | **2** | 2 |
| | **5,473** | 5,828 |

There was no interest income accrued on impaired loans two or more months in arrears (2016: £0)

## 3. Interest payable and similar charges

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| On shares held by individuals | **1,746** | 1,940 |
| On deposits and other borrowings | **107** | 89 |
| On subordinated liabilities | **23** | 57 |
| | **1,876** | 2,086 |

## 4. Administrative expenses

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| Wages and salaries | **994** | 981 |
| Social security costs | **110** | 101 |
| Other pension costs | **78** | 100 |
| | **1,182** | 1,182 |
| Other administrative expenses | **1,196** | 1,035 |
| | **2,378** | 2,217 |

The remuneration of the External Auditor, which is included within administrative costs above, is set out below (excluding VAT):

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| Audit of these annual accounts | **49** | 40 |
| | **49** | 40 |

Following changes to EU audit legislation in 2016, the Society, like all building societies, is now designated a Public Interest Entity (PIE). The PIE designation has additional audit requirements, which is the main reason why there is a significant increase in external audit fees for 2017.

## 5. Employee numbers

The average number of persons employed by the Society (including directors) during the year, analysed by category, was as follows:

| | **2017** | 2016 |
|---|---|---|
| Full time | **25** | 26 |
| Part time | **3** | 2 |
| | **28** | 28 |

## 6. Directors' remuneration

Full details are given in the Directors' Remuneration Report. Total remuneration amounted to £261,000 (2016: £246,000).
In addition, payment of £11,769 (2016: £8,000) is due to Walker Morris LLP for the services of Louise Power. Full details are given in the table within the Remuneration Report on pages 22-24.

## 7. Taxation

| | **2017** | 2016 |
|---|---|---|
| | **£000** | £000 |
| *Current tax* | | |
| Current tax on income for the period | **207** | 180 |
| Adjustments in respect of prior periods | **(1)** | (12) |
| Total current tax | **206** | 168 |
| *Deferred tax see note 20* | | |
| Origination and reversal of timing differences | **(11)** | 25 |
| Adjustment in respect of previous periods | **1** | 10 |
| Change in tax rate | **1** | (5) |
| Total deferred tax | **(9)** | 30 |
| Tax expenses (income) relating to changes in accounting policies | | – |
| | **197** | 198 |

*Analysis of current tax recognised in profit and loss*

| | **2017** | 2016 |
|---|---|---|
| | **£000** | £000 |
| Profit for the year | **915** | 920 |
| Total tax expense | **197** | 198 |
| Profit excluding taxation | **1,112** | 1,118 |
| Tax using the UK corporation tax rate of 20.00% (2016: 20.00%) | **214** | 224 |
| Community investment relief | **(25)** | (25) |
| Reduction in tax rate on deferred tax balances | **1** | (5) |
| Non-deductible expenses | **7** | 6 |
| Under / (over) provided in prior years | **–** | (2) |
| Total tax expense included in profit or loss | **197** | 198 |

The effective tax rate for the twelve month period ended 31 December 2017 is 19.25%. This differs from the standard rate of corporation tax in the UK due to the impact of disallowable expenditure, deferred tax movement and adjustments for prior years.

Adjustments to tax changes in earlier years arise because the tax charge in the financial statements is estimated before the detailed corporation tax calculations are prepared. Additionally, HM Revenue & Customs may not agree with the tax return that was submitted for a year and the tax liability for a previous year may be adjusted as a result.

Some expenses incurred by the Society may be entirely appropriate charges for inclusion in its financial statements but are not allowed as a deduction against taxable income when calculating the Society's tax liability. The most significant example of this is accounting depreciation or losses incurred on assets that do not qualify for capital allowances (generally land and buildings). Other examples include some legal expenses and some repair costs.

## 8. Cash and cash equivalents

| | **2017**<br>**£000** | 2016<br>£000 |
|---|---|---|
| Cash in hand and balances with the Bank of England | **41,614** | 36,192 |
| Loans and advances to credit institutions (see note 9) | **8,487** | 6,113 |
| Cash and cash equivalents per cash flow statements | **50,101** | 42,305 |

## 9. Loans and advances to credit institutions

| | **2017**<br>**£000** | 2016<br>£000 |
|---|---|---|
| Accrued interest | **18** | 4 |
| Repayable on demand | **6,976** | 5,611 |
| In not more than three months | **1,500** | 500 |
| In not more than one year | **3,000** | 1,000 |
| Total loans and advances to credit institutions | **11,494** | 7,115 |
| Total included within cash and cash equivalents | **8,487** | 6,113 |

## 10. Debt securities

| | 2017 £000 | 2016 £000 |
|---|---|---|
| Gilts | **2,017** | – |
| Treasury bills | **3,998** | 8,496 |
| Certificates of deposit | **1,503** | – |
| | **7,518** | 8,496 |
| Debt securities have remaining maturity as follows: | | |
| In not more than one year | **7,518** | 8,496 |
| | **7,518** | 8,496 |
| Transferable debt securities comprise: | | |
| Listed on a recognized investment exchange | **2,017** | – |
| Unlisted | **5,501** | – |
| | **7,518** | – |
| Market value of listed transferable debt securities | **2,011** | – |

Movements in debt securities during the year (excluding accrued interest) are summarised as follows:

| | 2017 £000 | 2016 £000 |
|---|---|---|
| At 1 January 2017 | **8,489** | 5,486 |
| Additions[1] | **12,077** | 17,003 |
| Disposals and maturities | **(13,063)** | (14,000) |
| At 31 December 2017 | **7,503** | 8,489 |

[1]No Treasury bills purchased in the year were acquired at a premium or a discount to their maturity values.

## 11. Loans and advances to customers

| | 2017 £000 | 2016 £000 |
|---|---|---|
| Loans fully secured on residential property | **105,817** | 109,570 |
| Loans fully secured on land | **8,585** | 8,409 |
| Other loans | **10** | 10 |
| | **114,412** | 117,989 |
| The remaining maturity of loans and advances to customers from the reporting date is as follows: | | |
| In not more than three months | **1,638** | 1,179 |
| In more than three months but not more than one year | **3,451** | 4,934 |
| In more than one year but not more than five years | **20,959** | 21,099 |
| In more than five years | **88,988** | 91,439 |
| | **115,036** | 118,651 |
| Less: allowance for impairment (note 12) | **624** | 662 |
| | **114,412** | 117,989 |

The maturity analysis above is based on contractual maturity adjusted for EIR but not for expected redemption levels.

Loans fully secured on land includes £2,481 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 the 1 October 1998 that are included in “loans fully secured on residential property” but is necessary to comply with the requirements of the Building Societies Act 1997.

## 12. Allowance for impairment

| Provision for impairment on loans and advances<br>At 1 January 2017 | Loans fully secured on residential property £000 | Other loans £000 | Total £000 |
|---|---|---|---|
| Individual impairment | 56 | 458 | 514 |
| Collective impairment | 144 | 4 | 148 |
| | 200 | 462 | 662 |
| Amounts written off during the year, net of recoveries | | | |
| Individual impairment | 18 | – | 18 |
| Collective impairment | – | – | – |
| | 18 | – | 18 |
| **Income statement** | | | |
| Impairment losses on loans and advances | | | |
| Individual impairment | (7) | (5) | (12) |
| Collective impairment | (18) | (2) | (20) |
| Adjustments to impairment losses on loans and advances resulting from recoveries during the year | | | |
| Individual impairment | – | (6) | (6) |
| Charge/(credit) for the year | (25) | (13) | (38) |
| **At 31 December 2017** | | | |
| **Individual impairment** | **49** | **447** | **496** |
| **Collective impairment** | **126** | **2** | **128** |
| | **175** | **449** | **624** |

| Provision for impairment on loans and advances<br>At 01 January 2016 | Loans fully secured on residential property £000 | Other loans £000 | Total £000 |
|---|---|---|---|
| Individual impairment | 65 | 233 | 298 |
| Collective impairment | 98 | 6 | 104 |
| | 163 | 239 | 402 |
| Amounts written off during the year, net of recoveries | | | |
| Individual impairment | – | – | – |
| Collective impairment | – | – | – |
| | – | – | – |
| **Income statement** | | | |
| Impairment losses on loans and advances | | | |
| Individual impairment | (9) | 231 | 222 |
| Collective impairment | 46 | (2) | 44 |
| Adjustments to impairment losses on loans and advances resulting from recoveries during the year | | | |
| Individual impairment | – | (6) | (6) |
| Charge/(credit) for the year | 37 | 223 | 260 |
| At 31 December 2016 | | | |
| Individual impairment | 56 | 458 | 514 |
| Collective impairment | 144 | 4 | 148 |
| | 200 | 462 | 662 |

## 13. Tangible fixed assets

| Cost | Land and buildings £000 | Fixtures, fittings & plant and machinery £000 | computer equipment £000 | Motor vehicles £000 | Total £000 |
|---|---|---|---|---|---|
| Balance at 1 January 2017 | 1,405 | 170 | 385 | 54 | 2,014 |
| Additions | – | 1 | 16 | – | 17 |
| Disposals | – | – | (23) | (1) | (24) |
| Balance at 31 December 2017 | 1,405 | 171 | 378 | 53 | 2,007 |
| **Depreciation** | | | | | |
| Balance at beginning of the year | 294 | 146 | 252 | 28 | 720 |
| Depreciation charge for the year | 25 | 5 | 43 | 13 | 86 |
| Disposals | – | – | (23) | (1) | (24) |
| Balance at 31 December 2017 | 319 | 151 | 272 | 40 | 782 |
| Net book value<br>At 1 January 2017 | 1,111 | 24 | 133 | 26 | 1,294 |
| **At 31 December 2017** | **1,086** | **20** | **106** | **13** | **1,225** |

Freehold land and buildings, which are included in the balance sheet at cost less depreciation, amounted to £1.086m at 31 December 2017 (2016: £1.111m). 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.

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

## 14. Investments

| Cost | Loans £000 | Other investments £000 | Total £000 |
|---|---|---|---|
| At 1 January 2017 | 1,548 | 69 | 1,617 |
| Additions | 490 | – | 490 |
| Repayments | (31) | – | (31) |
| At 31 December 2017 | 2,007 | 69 | 2,076 |
| **Impairment** | | | |
| At 1 January 2017 | – | (8) | (8) |
| Impairment losses/gains | – | (8) | (8) |
| At 31 December 2017 | – | (16) | (16) |
| **Net book value**<br>**At 31 December 2017** | **2,007** | **53** | **2,060** |
| At 1 January 2017 | 1,548 | 61 | 1,609 |

The Society continues to invest directly in renewable energy as announced at the 2014 AGM, and to support other co-operative ventures. All loans are interest bearing and as at 31 December 2017 no loan is considered to be impaired.

**Analysis of investments by carrying value**

| **Investments - Basic** | **2017 opening carrying value £000** | Additions £000 | Repayment of capital £000 | Impairment £000 | 2017 closing carrying value £000 |
|---|---|---|---|---|---|
| Ecossol PV | 190 | – | 14 | – | 176 |
| Oakapple Berwickshire | 229 | – | 13 | – | 216 |
| Monnow Valley CHP | 250 | – | – | – | 250 |
| Atlantis Ocean Energy | 250 | – | – | – | 250 |
| Co-operative and Community Finance | 500 | – | – | – | 500 |
| MVT | 129 | – | – | – | 129 |
| **Total** | **1,548** | **–** | **27** | **0** | **1,521** |

| **Investments - Non-basic** | **2017 opening carrying value £000** | Additions £000 | Repayment of capital £000 | Movement in Fair Value £000 | 2017 closing carrying value £000 |
|---|---|---|---|---|---|
| Upper Pitforthie Windgen* | – | 250 | 4 | – | 246 |
| United Downs Geothermal* | – | 240 | – | – | 240 |
| Ethical Properties | 10 | – | – | 3 | 7 |
| Phone Co-op | 12 | – | – | – | 12 |
| MVT | 5 | – | – | – | 5 |
| SFRE | 34 | – | – | 5 | 29 |
| **Total** | **61** | **490** | **4** | **8** | **539** |

* It is our policy to hold non-basic investments at fair value but in the case of Upper Pitforthie Windgen and United Downs Geothermal we consider the fair value to be equivalent to the carrying value.

## 15. Intangible assets

| Cost | Purchased software £000 | Total £000 |
|---|---|---|
| Balance at 01 January 2017 | 234 | 234 |
| Balance at 31 December 2017 | 234 | 234 |
| **Amortisation** | | |
| Balance at 01 January 2017 | 131 | 131 |
| Amortisation for the year | 35 | 35 |
| Balance at 31 December 2017 | 166 | 166 |
| Net book value<br>At 01 January 2017 | 103 | 103 |
| **At 31 December 2017** | **68** | **68** |

## 16. Other debtors

| | **2017 £000** | 2016 £000 |
|---|---|---|
| Prepayments | **257** | 246 |
| Accrued income | **14** | 12 |
| | **271** | 258 |

Debtors include prepayments and accrued income of £5,192 (2016:£2,000) for the Society that are due after more than one year.

## 17. Shares

| | **2017 £000** | 2016 £000 |
|---|---|---|
| Held by individuals | **157,603** | 153,701 |
| Shares are repayable with remaining maturities from the balance sheet date as follows: | | |
| Accrued interest | **497** | 656 |
| On demand | **137,781** | 133,005 |
| In not more than three months | **19,325** | 20,040 |
| | **157,603** | 153,701 |

## 18. Amounts owed to other customers

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| | **10,171** | 9,375 |
| Repayable on demand | **10,171** | 9,375 |

## 19. Other liabilities

| | 2017<br>£000 | 2016<br>£000 |
|---|---|---|
| Corporation tax | **207** | 179 |
| Other creditors | **153** | 157 |
| | **360** | 336 |

## 20. Deferred tax assets and liabilities

Deferred tax assets and liabilities are attributable to the following:

| | Assets<br>2017<br>£000 | 2016<br>£000 | Liabilities<br>2017<br>£000 | 2016<br>£000 | Net<br>2017<br>£000 | 2016<br>£000 |
|---|---|---|---|---|---|---|
| Accelerated capital allowances | **–** | – | **54** | 67 | **54** | 67 |
| FRS 102 transitional adjustments | **(15)** | (18) | **–** | – | **(15)** | (18) |
| Other timing differences | **(10)** | (12) | **–** | – | **(10)** | (12) |
| Tax (assets) / liabilities | **(25)** | (30) | **54** | 67 | **29** | 37 |

During the year beginning 1 January 2018, the net reversal of deferred tax assets and liabilities is expected to decrease the corporation tax charge for the year by approximately £3,000. This is due to the reversal of a deferred tax asset recognised in relation to the FRS 102 transitional adjustments. The corporation tax impact of the EIR transitional adjustments is spread over ten years and so deferred tax has been recognised accordingly.

The accounting treatment of expenditure on fixed assets differs from the taxation treatment. For accounting purposes, an annual rate of depreciation is applied by the Society. For taxation purposes, the Society is able to claim capital allowances, a tax relief provided in law.

This difference between the rates of depreciation and capital allowances means that there is a difference between the taxable profit for accounting and taxation purposes and this year the Society was able to claim more tax relief than the accounting charge for depreciation.

## 21. Provisions

| | Other provisions £000 | FSCS levy £000 | Total £000 |
|---|---|---|---|
| Balance at 01 January 2017 | 43 | 25 | 68 |
| Paid in year | (66) | (24) | (90) |
| Charge for the year | 27 | 13 | 40 |
| **Balance at 31 December 2017** | **4** | **14** | **18** |

At 31 December 2017 the Society has a provision of £13,688 comprising management expenses levies for the Financial Services Compensation Scheme year 2017/2018. This is expected to be paid in April 2018.

Other provisions represent the remaining payments due for customer redress arising from the issue we identified during 2016 in the way that we had applied historic home insurance premiums to some members' mortgage accounts. The Society believes that some of the documentation in regard to the treatment of insurance premiums may have been misleading and has taken steps to rectify this error and pay appropriate redress and compensation.

## 22. Subordinated liabilities

| | **2017 £000** | 2016 £000 |
|---|---|---|
| Floating rate subordinated liabilities due 2019 | **750** | 750 |
| | **750** | 750 |
| Less unamortised premiums and issue costs | **(1)** | (1) |
| | **749** | 749 |

The Note is repayable at the date stated or earlier at the option of the Society with the prior consent of the PRA. The subordinated liability is denominated in sterling. Interest payments made on the floating rate loan is at a rate agreed with reference to the Bank of England Base Rate. 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 liability held by the Society £0.224m is permissible as Tier 2 capital resources.

# 23. Financial instruments

The Society uses financial instruments to invest liquid asset balances and raise wholesale funding.

The Society does not run a trading book.

***Categories of financial assets and liabilities***

Financial assets and liabilities are measured on an ongoing basis either at fair value or at amortised cost. Note 1.5 'Financial instruments' describes how the classes of financial instruments are measured, and how income and expenses, including fair value gains and losses, are recognised. The tables below analyse the Society's assets by financial classification:

| Carrying values by category 31 December 2017 | Held at amortised cost £000 | Held at fair value £000 | Total £000 |
|---|---|---|---|
| **Financial assets** | | | |
| Cash in hand and balances with the Bank of England | 41,614 | – | 41,614 |
| Treasury Bills and similar securities | 3,998 | – | 3,998 |
| Loans and advances to credit institutions | 11,494 | – | 11,494 |
| Debt Securities | 3,520 | – | 3,520 |
| Loans and advances to customers | 114,412 | – | 114,412 |
| Fixed asset investments | 1,522 | 538 | 2,060 |
| **Total financial assets** | **176,560** | **538** | **177,098** |
| Non-financial assets | 1,564 | – | 1,564 |
| **Total assets** | **178,124** | **538** | **178,662** |
| **Financial liabilities** | | | |
| Shares | 157,603 | – | 157,603 |
| Amounts owed to credit institutions | – | – | – |
| Amounts owed to other customers | 10,171 | – | 10,171 |
| Subordinated liabilities | 749 | – | 749 |
| Other liabilities | 360 | – | 360 |
| **Total financial liabilities** | **168,883** | **–** | **168,883** |
| Non-financial liabilities and Reserves | 9,779 | – | 9,779 |
| **Total liabilities** | **178,662** | **–** | **178,662** |

## 23. Financial instruments (continued)

| Carrying values by category<br>31 December 2016 | Held at amortised cost<br>£000 | Held at Fair value | Total<br>£000 |
|---|---|---|---|
| **Financial assets** | | | |
| Cash in hand and balances with the Bank of England | 36,192 | – | 36,192 |
| Treasury Bills and similar securities | 8,496 | – | 8,496 |
| Loans and advances to credit institutions | 7,115 | – | 7,115 |
| Loans and advances to customers | 117,989 | – | 117,989 |
| Fixed asset investments | 1,298 | 311 | 1,609 |
| **Total financial assets** | **171,090** | **311** | **171,401** |
| Non-financial assets | 1,655 | – | 1,655 |
| **Total assets** | **172,745** | **311** | **173,056** |
| **Financial liabilities** | | | |
| Shares | 153,701 | – | 153,701 |
| Amounts owed to credit institutions | – | – | – |
| Amounts owed to other customers | 9,375 | – | 9,375 |
| Subordinated liabilities | 749 | – | 749 |
| Other liabilities | 336 | – | 336 |
| **Total financial liabilities** | **164,161** | **–** | **164,161** |
| Non-financial liabilities | 8,895 | – | 8,895 |
| **Total liabilities** | **173,056** | **–** | **173,056** |

At 31 December 2017, the Society has loan commitments of £19.0m (2016: £11.5m) measured at cost less impairment.

***Valuation of financial instruments carried at fair value***

The Society holds certain financial assets and liabilities at fair value, grouped into Levels 1 to 3 of the fair value hierarchy (see below).

*Valuation techniques*

Fair values are determined using the following fair value hierarchy that reflects the significance of the inputs in measuring fair value:

Level 1 The most reliable fair values of financial instruments are quoted market prices in an actively traded market. The Society's Level 1 portfolio mainly comprises financial fixed asset investments for which traded prices are readily available.

Level 2 These are valuation techniques for which all significant inputs are taken from observable market data. These include valuation models used to calculate the present value of expected future cash flows and may be employed when no active market exists and quoted prices are available for similar instruments in active markets.

Level 3 These are valuation techniques for which one or more significant input is not based on observable market data. Valuation techniques include net present value by way of discounted cash flow models.

## 23. Financial instruments (continued)

The table below summarises the fair values of the Society's financial assets and liabilities that are accounted for at fair value, analysed by the valuation methodology used by the Society to derive the financial instruments' fair value:

| | Level 1<br>£000 | Level 2<br>£000 | Level 3<br>£000 | Total<br>£000 |
|---|---|---|---|---|
| 31 December 2017 | | | | |
| **Financial assets** | | | | |
| Fair value through profit and loss | 7 | 28 | 503 | 538 |
| | 7 | 28 | 503 | 538 |
| **Financial liabilities** | | | | |
| Fair value through profit and loss | – | – | – | – |
| | – | – | – | – |
| 31 December 2016 | | | | |
| **Financial assets** | | | | |
| Fair value through profit and loss | 10 | 34 | 250 | 294 |
| | 10 | 34 | 250 | 294 |
| **Financial liabilities** | | | | |
| Fair value through profit and loss | – | – | – | – |
| | – | – | – | – |

Credit risk is the risk that a borrower or counterparty of the Society will cause a financial loss for the Society by failing to discharge their contractual obligation.

Changes in the credit quality and the recoverability of loans and amounts due from counterparties influence the Society's exposure to credit risk. The Society maintains a cautious approach to credit risk and new lending. All loan applications are assessed with reference to the Society's Lending Policy.

Changes to the Policy are approved by the Board and the approval of loan applications is mandated. The Board is responsible for approving treasury counterparties.

Adverse changes in the credit quality of counterparties, deterioration in the wider economy, including rising unemployment, changes in interest rates, deterioration in household finances and any contraction in the UK property market leading to falling property values, could affect the recoverability and value of the Society's assets and impact its financial performance. An economic downturn and fall in house prices would affect the level of impairment losses.

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-. Assets and Liabilities Committee (ALCO), the Board Lending Committee and the Board provide oversight to the effectiveness of the Society's credit management and the controls in place ensure lending is within the Board approved credit risk appetite.

## 23. Financial instruments (continued)

The Society's maximum credit risk exposure is detailed in the table below:

| | 2017 £000 | 2016 £000 |
|---|---|---|
| Cash with Bank of England | **41,614** | 36,192 |
| Loans and advances to credit institutions | **11,494** | 7,115 |
| Debt securities | **3,520** | – |
| Treasury Bills | **3,998** | 8,496 |
| Loans and advances to customers | **115,036** | 118,651 |
| Total statement of financial position exposure | **175,662** | 170,454 |
| Off balance sheet exposure – mortgage commitments | **18,992** | 11,529 |
| | **194,654** | 181,983 |

The Society does not use credit derivatives, or similar instruments, to manage its credit risk.

# 23. Financial instruments (continued)

*Credit quality analysis of loans and advances to customers*

The table below sets out information about the credit quality of financial assets and the allowance for impairment/loss held by the Society against those assets.

| | **2017 Loans fully secured on residential property £000** | **Loans fully secured on land £000** | **Other loans £000** | 2016 Loans fully secured on residential property £000 | Loans fully secured on land £000 | Other loans £000 |
|---|---|---|---|---|---|---|
| **Neither past due nor impaired** | **105,042** | **7,025** | **10** | 108,405 | 6,828 | 10 |
| **Past due but not impaired** | | | | | | |
| 1 – 2 months | **543** | **–** | **–** | 799 | 25 | – |
| 2 – 3 months | **1** | **–** | **–** | 94 | – | – |
| Greater than 3 months | **96** | **9** | **–** | 131 | – | – |
| | **640** | **9** | **–** | 1,024 | 25 | – |
| **Individually impaired** | | | | | | |
| Not past due | **135** | **1,551** | **–** | 141 | 1,556 | – |
| 1 – 2 months | **–** | **–** | **–** | – | – | – |
| 2 – 3 months | **–** | **–** | **–** | – | – | – |
| Greater than 3 months | **–** | **–** | **–** | – | – | – |
| | **135** | **1,551** | **–** | 141 | 1,556 | – |
| **Allowance for impairment** | | | | | | |
| Individual | **49** | **447** | **–** | 56 | 458 | – |
| Collective | **126** | **2** | **–** | 144 | 4 | – |
| **Total allowance for impairment** | **175** | **449** | **–** | 200 | 462 | – |

Individual assessments are made of all mortgage loans where objective evidence indicates that losses are likely (for example when loans are past due) or the property is in possession, or where fraud, negligence or the borrower has significant financial difficulties has been identified. Further consideration is given in accounting policy 1.5 to the accounts.

## 23. Financial instruments (continued)

The table below stratifies credit exposures from mortgage loans and advances to retail customers by ranges of loan-to-value (LTV) ratio. LTV is calculated as the ratio of the gross amount of the loan – or the amount committed for loan commitments – to the value of the collateral. The gross amounts exclude any impairment allowance. The valuation of the collateral excludes any adjustments for obtaining and selling the collateral. The value of the collateral for residential mortgage loans is based on the collateral value at origination updated based on changes in house price indices.

| LTV ratio | 2017 £000 | 2016 £000 |
|---|---|---|
| Less than or equal to 50% | **43,921** | 46,761 |
| Greater than 50% but less than or equal to 70% | **35,707** | 38,721 |
| Greater than 70% but less than or equal to 90% | **33,661** | 31,765 |
| Greater than 90% but less than or equal to 100% | **1,863** | 1,526 |
| Greater than 100% | **–** | – |
| | **115,152** | 118,773 |

*Forbearance*

The Society exercises forbearance to assist borrowers who, due to personal and financial circumstances, are experiencing difficulty in meeting their contractual repayments. The Society, wherever possible, arranges for a concession to be put in place by way of a payment holiday, or repayment of interest only, for an agreed period of time. Consideration is also given to borrowers in arrears and appropriate arrangements are agreed to underpay, or overpay, the arrears within an agreed timeframe. When a borrower enters into a forbearance arrangement regular monitoring of the account is undertaken and consideration is given to the ongoing potential risk to the Society and the suitability of the arrangement for the borrower. An individual provision is made against any loan that is considered to be impaired. Once the agreement has been successfully concluded the case is no longer considered to be impaired but continues to be monitored.

The table below analyses residential mortgage balances with renegotiated terms at the year end:

| | 2017 £000 | 2016 £000 |
|---|---|---|
| Payment holiday | **1,162** | 1,586 |
| Interest only | **1,687** | 1,101 |
| Arrears overpayment | **–** | 3 |
| Arrears underpayment | **96** | – |
| | **2,945** | 2,690 |

There were a total of 14 accounts in forbearance at 31 December 2017 (2016: 16).

There was one individual impairment provision required where the loan is not in arrears but is considered to be impaired (2016: 1).

# 23. Financial instruments (continued)

***Liquidity risk***

Liquidity risk is the risk that the Society will not have sufficient financial resources available to meet its obligations as they fall due under normal business conditions or a stressed environment. The Society's Liquidity Policy requires that a significant amount of its assets are carried in the form of on-call and other readily available assets in order to:

- Meet day-to-day business needs
- Meet any unexpected funding stress scenario
- Ensure maturity mismatches are provided for

Balance sheet and liquidity limits (including counterparty limits) are set to support this risk appetite within the Society's Financial Risk Policy.

Monitoring of liquidity is performed daily. Compliance with policy is reported to every ALCO and monthly to the Board.

The Society's Liquidity Policy is designed to ensure that the Society has sufficient liquid resources to withstand a range of scenarios. A series of liquidity stresses have been developed as part of the Society's Individual Liquidity Adequacy Assessment (ILAAP). They include scenarios that fulfil the specific requirements of the Prudential Regulation Authority (PRA), the Society specific, market-wide and a combination of both scenarios. The stress tests are performed periodically and reported to ALCO to confirm that the liquidity policy remains appropriate.

The Society's liquid resources comprise of high quality liquid assets, including a Bank of England Reserve Accounts, term deposit accounts, or in debt securities and treasury bills that are capable of being sold at short notice to meet unexpected adverse cash flows.

All Society liquid assets are unencumbered as at the balance sheet date.

*Maturity analysis for financial assets and financial liabilities*

The tables below set out the carrying value of the Society's financial assets and financial liabilities. In practice, contractual maturities are not always reflected in actual experience. For example, loans and advances to customers tend to repay ahead of contractual maturity and customer deposits (for example, shares) are likely to be repaid later than on the earliest date on which repayment can be required.

The following analysis shows gross contractual flows payable under financial liabilities. This includes interest accrued at current rates for the average period until maturity on the amounts outstanding at the financial position date.

| **31 December 2017** | **On demand £000** | **Not more than three months £000** | **More than three months but not more than one year £000** | **More than one year but not more than five years £000** | **More than five years £000** | **Total £000** |
|---|---|---|---|---|---|---|
| Shares | 138,278 | 19,389 | – | – | – | 157,667 |
| Amounts owed to other customers | 10,171 | – | – | – | – | 10,171 |
| Subordinated liabilities | – | – | – | 783 | – | 783 |
| **Total financial liabilities** | **148,449** | **19,389** | **–** | **783** | **–** | **168,621** |

## 23. Financial instruments (continued)

| 31 December 2016 | On demand £000 | Not more than three months £000 | More than three months but not more than one year £000 | More than one year but not more than five years £000 | More than five years £000 | Total £000 |
|---|---|---|---|---|---|---|
| Shares | 133,661 | 20,106 | – | – | – | 153,767 |
| Amounts owed to other customers | 9,375 | – | – | – | – | 9,375 |
| Subordinated liabilities | – | – | – | 806 | – | 806 |
| Total financial liabilities | 143,036 | 20,106 | – | 806 | – | 163,948 |

***Market risk***

Market risk is the risk that the value of, or income arising from, the Society's assets and liabilities changes as a result of changes in market prices, the principal elements being interest rate risk, foreign currency risk and equity risk.

As the Society only deals with products in sterling it is not exposed to foreign currency risk. The Society's products are also only interest orientated products so are not exposed to other pricing risks. The level of equity risk is not material.

The Society monitors interest rate risk exposure against limits by determining the effect on the Society's current net notional value of assets and liabilities for a parallel shift in interest rates equivalent to 200 basis points (bps) or 2% for all maturities, in line with regulatory requirements. The results are measured against the risk appetite for market risk which is currently set at a maximum of 4% of capital. Results are reported to ALCO and the Board on a bi-monthly basis.

The following table provides an analysis of the Society's sensitivity to an increase or decrease in market interest rates, assuming no asymmetrical movement in yield curves and a constant financial position.

| Sensitivity of reported equity to interest rate movements | 200bp parallel increase £000 | 200bp parallel decrease £000 |
|---|---|---|
| **2017** | | |
| **At 31 December** | | |
| **Average for the period** | **154** | **165** |
| **Maximum for the period** | **206** | **217** |
| **Minimum for the period** | **109** | **116** |
| 2016 | | |
| At 31 December | | |
| Average for the period | 120 | 130 |
| Maximum for the period | 148 | 160 |
| Minimum for the period | 82 | 88 |

# 23. Financial instruments (continued)

***Capital***

The Society's policy is to maintain a strong capital base to maintain member, creditor and market confidence and to sustain future development of the business. The formal ICAAP process (Internal Capital Adequacy Assessment Process) assists the Society with its management of capital. The Board monitors the Society's capital position on a monthly basis to assess whether adequate capital is held to mitigate the risks it faces in the course of its business activities. The Society's actual and expected capital position is reviewed against stated risk appetite which aims to maintain capital at a specific level above its Internal Capital Guidance (ICG).

The Board manages the Society's capital and risk exposures to maintain capital in line with regulatory requirements which includes monitoring of:

- **Lending decisions** – The Society maintains a comprehensive set of sectoral limits on an overall and 12-month rolling basis to manage credit risk appetite. Individual property valuations are monitored against House Price Index (HPI) data and updated quarterly
- **Concentration risk** – The design of lending products takes into account the overall mix of the loan portfolio to manage exposure to risks arising from the property market and other markets the Society is active in
- **Counterparty risk** – Wholesale lending is only carried out with approved counterparties in line with the Society's lending criteria (including ethical considerations) and is subject to a range of limits that reflect the risk appetite of the Society

Stress tests are used as part of the process of managing capital requirements.

The Society's capital requirements are set and monitored by the Prudential Regulation Authority (PRA). During 2017 the Society has continued to comply with the EU Capital Requirements Regulation and Directive (Basel III) as amended by the PRA. Further details of the Society's approach to Risk Management are given in the Directors' Report under Principal Risks and Uncertainties.

Regulatory capital is analysed into two tiers:

- **Tier 1 capital** – which is currently comprised solely of retained earnings
- **Tier 2 capital** – which includes subordinated liabilities and collective provisions

The level of capital is matched against risk-weighted assets which are determined according to specified requirements that seek to reflect the varying levels of risk attached to assets.

There were no reported breaches of capital requirements during the year. There have been no material changes in the Society's management of capital during the year.

| | Note | **2017 £000** | 2016 £000 |
|---|---|---|---|
| **Tier 1 Capital** | | | |
| General reserve | | **9,595** | 8,680 |
| Less intangibles | 15 | **(56)** | (86) |
| **Total Tier 1 Capital** | | **9,539** | 8,594 |
| **Tier 2 Capital** | | | |
| Subordinated liabilities | 23 | **224** | 374 |
| Collective provision | 12 | **128** | 148 |
| **Total Tier 2 Capital** | | **352** | 522 |
| **Total Regulatory Capital** | | **9,891** | 9,116 |

## 24. Contingencies

There were no contingencies required as at the end of December 2017.

## 25. Related parties

*Transactions with key management personnel*

Key management personnel consists of the Executive Directors and Non-Executive Directors who are responsible for ensuring that the Society meets its strategic and operational objectives. In the normal course of business, key management personnel, and their close family members, transacted with the Society. The balances of transactions with key management personnel, and their close family members, are as follows:

| | **Number of key management personnel and their close family members 2017** | **Amounts in respect of key management personnel and their close family members 2017 £000** | Number of key management personnel and their close family members 2016 | Amounts in respect of key management personnel and their close family members 2016 £000 |
|---|---|---|---|---|
| Loans and advances to customers | **2** | **249** | 2 | 264 |
| Deposits and share accounts | **13** | **145** | 10 | 99 |

**Directors' loans and transactions**

At 31 December 2017 there were two outstanding mortgage loans (2016: 2), made in the ordinary course of the Society's business to Directors and connected persons, amounting to £248,938 (2016: £263,919).

A register is maintained by the Society containing details of transactions and agreements made between the Society and the Directors and their connected persons. A register of loans to Directors and connected persons is maintained under Section 68 of the Building Societies Act 1986 at the Society's head office. This is available for inspection during normal office hours for a period of 15 days prior to, and at, the Society's Annual General Meeting.

At the end of 2016 Steve Round, CEO of Saescada, entered into a contract with the Society to review Digital Strategy at an agreed fee of £24,000 including VAT. The review was completed early 2017.

*Other related party transactions*

During the year the Society donated £10,000 to the Ecology Building Society Charitable Foundation.

At the beginning of the year the Society held an existing loan of £129,000 made to Mutual Vision Technology, the provider of the Society's IT services. The Society has received interest on the loan amounting to £1,935 (2016: £1,935) and fees of £3,044 (2016: 2,984) in relation to the services of P.C. Ellis as a director..

## 26. Subsequent events

There have been no material subsequent events between 31 December 2017 and the approval of this Annual Report and Accounts by the Board.

## 27. Country-by-country reporting

The reporting obligations set out in Article 89 of the European Union's Capital Requirements Directive IV (CRD IV) have been implemented in the UK by the Capital Requirements (Country-by-Country Reporting) Regulations 2013. The purpose of these regulations is to provide clarity on the Society's income and the locations of its operations.

### For the year ended 31 December 2017:

- The Society's principal activities are mortgage lender and provider of savings accounts
- The Society's turnover (defined as net interest receivable) was £3.597m (2016: £3.742m). Profit before tax £1.112m (2016: £1.118m) all of which arose from UK-based activity
- Number of employees was 28 (2016: 28)
- Corporation tax of £0.178m (2016: £0.207m) was paid in the year and is within the UK tax jurisdiction
- No public subsidies were received in the year

# Annual business statement

Year ended 31 December 2017

### 1 Statutory percentages

| | Statutory limit<br>% | **At 31 December 2017**<br>**%** | At 31 December 2016<br>% |
|---|---|---|---|
| Lending limit | 25.00 | **9.68** | 8.90 |
| Funding limit | 50.00 | **3.50** | 3.20 |

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

| | **2017**<br>**%** | 2016<br>% |
|---|---|---|
| Gross capital as a percentage of shares and borrowings | **5.85** | 5.53 |
| Free capital as a percentage of shares and borrowings | **5.16** | 4.76 |
| Liquid assets as a percentage of shares and borrowings | **36.14** | 31.77 |
| Profit after taxation as a percentage of mean total assets | **0.52** | 0.58 |
| Management expenses as a percentage of mean total assets | **1.42** | 1.45 |

Gross capital represents the general reserves and subordinated liabilities. Of the subordinated liability shown on the statement of financial position, £0.224m is classed as Tier 2 capital.

Free capital is the gross capital plus the collective impairment for losses on loans less tangible and intangible fixed assets.

Shares and borrowings are the aggregate of shares, amounts owed to credit institutions and amounts owed to other customers including accrued interest.

Liquid assets are taken from the items so named in the statement of financial position.

The profit after taxation is the profit for the year as shown in the statement of comprehensive income

Management expenses are the administrative expenses plus depreciation and amortisation for the year as shown in the statement of comprehensive income.

Mean total assets are the average of the 2017 and 2016 total assets.

### 3 Information relating to Directors at 31 December 2017

| Name and date of birth | Occupation and date of appointment to the Board | Other directorships |
|---|---|---|
| **Steven John Round**<br>08.04.1960 | Managing Director<br>09.12.2010 | Strategic Intent Ltd<br>Change Account Ltd<br>Saescada Limited |
| **Paul Charles Ellis**<br>10.09.1957 | Building Society Chief Executive<br>05.05.1984 | INAISE (International Association of Investors in the Social Economy)<br>Mutual Vision Technologies Ltd<br>Friends of Gledhow Valley Woods |
| **Pamela Waring**<br>12.06.1956 | Building Society Finance Director and Secretary<br>07.06.2000 | Home-Start Craven |
| **Timothy David Morgan**<br>08.12.1964 | Finance Director and Company Secretary<br>28.08.2013 | Ecology Building Society Charitable Foundation<br>Shared Interest Society Ltd<br>Northern Dance |
| **Christopher Jon Newman**<br>06.09.1976 | Commercial Director and Company Secretary<br>27.09.2013 | Parity Projects Ltd |
| **Alison Vipond**<br>06.02.1973 | Environmentalist & Researcher<br>27.09.2013 | Ecology Building Society Charitable Foundation<br>Electrozest Limited |
| **Andrew John Gold**<br>30.12.1969 | Director and Risk, Audit & Compliance Professional<br>30.05.2014 | Airedale NHS Foundation Trust |
| **Louise Power**<br>20.04.1969 | Solicitor<br>17.06.2015 | Walker Morris LLP |
| **Vincent Smith**<br>29.09.1959 | Assistant Treasurer<br>03.11.2017 | None |

Paul Ellis and Pam Waring both have service contracts, details of which can be found in the Directors' Remuneration Report on pages 22-24. There are no extended notice terms included in these contracts.

Documents may be served on the above Directors and should be marked 'private and confidential' c/o Financial Services Audit, KPMG LLP, 1 Sovereign Square, Leeds LS1 4DA

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