Annual Report and Accounts

Year ended 31 March 2017

the West Brom

Contents

Key highlights of the 2016/17 financial year

£712m

Gross residential mortgage lending of **£712m** (2015/16: £673m) and a **15%** (2015/16: 25%) growth in the prime owner occupied book

£4.4bn

Members' savings balances maintained at **£4.4bn** (2015/16: £4.4bn), with residential mortgages covered 1.04 times (2015/16: 1.06 times) by retail deposits

underlying profit up 60%

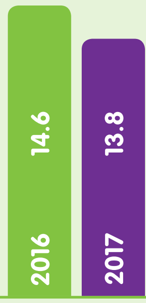
Underlying profit before tax **up 60%** to £7.7m (2015/16: £4.8m)

£19.8m Statutory loss

Statutory loss before tax of **£19.8m** (2015/16: profit of £13.5m), including costs of £27.5m relating to a one-off reimbursement of interest charged on certain buy to let mortgages

£5.8bn

Total assets stable at **£5.8bn** (2015/16: £5.8bn), with the increase in the residential mortgage book offsetting a 14% reduction in non-core commercial balances



13.8%

Robust capital position, with a Common Equity Tier 1 capital ratio of **13.8%** (2015/16: 14.6%) and a particularly strong leverage ratio of **6.8%** (2015/16: 7.6%)

Financial Adviser Service Awards

Development of the intermediary strategy to support future growth – received a five star rating, the highest accolade possible, for our service to mortgage brokers in the 2016 Financial Adviser Service Awards

Midlands and Yorkshire Contact Centre Awards

Recognition of achievement and innovation in customer service – winner of the 2016 Improvement Strategy of the Year category in the Midlands and Yorkshire Contact Centre Awards

Mortgage Finance Gazette Awards

Strong support for our local communities through fundraising, affinity partnerships, volunteering and outreach work – Highly Commended in the Community Services and Best Regional Building Society categories in the 2017 Mortgage Finance Gazette Awards

Chairman's Statement

In a year of upheaval and resultant economic uncertainty, I am pleased to report another year of strong underlying business performance and a robust capital base for future growth.

In my report last year I highlighted that we have re-established ourselves as a leading traditional building society. We have built on this progress, evidenced by a 70% growth in prime residential lending balances since we shifted our strategic focus to this segment of the housing sector four years ago. During the same period, buy to let lending and non-core commercial lending balances have reduced by 27% and 46% respectively.

The Group loss before tax of £19.8m (2015/16: profit of £13.5m) included the impact of refunding interest on certain buy to let loans, following the Court of Appeal's well-publicised decision to overturn a previous High Court ruling. Stripping out the one-off costs of this reimbursement, the underlying profit before tax was £7.7m (2015/16: £4.8m, excluding the additional interest charged on the affected buy to let loans), a 60% improvement year on year.

The Board decision to increase the interest rate paid by the landlord investors, the vast majority of whom were not members of the Society, was taken to address the unfair position of members given the low returns being suffered by the Society's saving members in this unprecedented low interest rate environment. The action was taken on the basis of clear and unambiguous legal advice. At no time were the Executive Directors incentivised or rewarded on the basis of the increase applied, and it was agreed at the outset that accordingly their remuneration would be unaffected by the reversal of the initial High Court decision. The challenges set for the Executive, against which their variable reward is assessed, are detailed in the Directors' Remuneration Report. The Society's key Common Equity Tier 1 capital ratio, although affected by the one-off interest refund, remains strong at 13.8% (2015/16: 14.6%). Full details of the year's performance are covered in the Chief Executive's Review and the Strategic Report.

Economic update

Although Article 50 has now been triggered, the full economic and political impact of Brexit (with, at the time of writing, a snap general election planned and renewed calls for a second referendum on Scottish independence) is still unclear. Initial post-Brexit concerns led to a sharp fall in the value of sterling and dampened business confidence. The Monetary Policy Committee reacted by cutting Bank Rate to 0.25% and launching the Bank of England's Term Funding Scheme (TFS), which provides lenders with very low cost funding in order to encourage growth. The resulting competition in the mortgage market has created excellent deals for borrowers but savers have, once again, been disappointed to see their returns diminish. We remain determined to do what we can to balance the conflicting demands of our depositing and borrowing members.

There has been some cooling in the housing market, with the rate of growth in house prices slowing in the early part of 2017. However, this may have some positive impact on those trying to buy their first home and may help maintain market stability. The Government has stated it intends to address the housing stock issue, recognising that there is high demand for affordable housing. A white paper, setting out its plans to boost the supply of new homes in England, was published in February 2017, which we generally support albeit, as we have fed back via the Building Societies Association, there are important initiatives that we believe would help achieve the aims of government, such as policies to discourage land from being held for too long without development and to increase the build out rates of the major housebuilders.

Regulatory matters

2016/17 saw no easing in the pace of regulatory change being driven by national and international authorities.

Further elements of the 'strengthening accountability in banking' framework, which was jointly implemented by the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA), were fully embedded during the year: The Certification Regime requires firms to assess the fitness and propriety of relevant employees and the Conduct Rules set out standards of behaviour that capture almost all staff working in the financial services sector.

In December 2016, the FCA published the terms of reference for its mortgages market study to explore whether borrowers are supplied with the tools and information needed to make informed choices. The findings are expected to be published during the next financial year.

The FCA has proposed a number of rules and guidelines in relation to the historic mis-selling of payment protection insurance (PPI), which include plans to lead a communications campaign and set a deadline by which complainants must submit their claim. We are supportive of the regulator's efforts to bring the matter to a fair and orderly conclusion. As part of its consultations, the FCA has sought to define circumstances whereby the levels of commission earned on PPI sales potentially gave rise to an 'unfair relationship'. The guidelines are sufficiently complex to warrant revisiting some past claims. The PPI provision disclosed in note 25 to the Accounts incorporates our expected obligations under the new rules.

A new accounting standard, IFRS 9 Financial Instruments, will fundamentally transform the way in which loan loss provisions are calculated and reported from 2018/19, requiring large-scale changes to systems and processes. IFRS 9 also has capital implications, particularly for those applying the Standardised Approach to credit risk as we do. We therefore welcome the European Banking Authority's (EBA's) proposals for transitional capital arrangements and the PRA's recent consultation which seeks to introduce fairness via revisions to the Pillar 2A capital framework.

Changes to the Board

Last year, Mark Gibbard informed the Board of his intention to retire at the end of 2016/17, after more than six years of service. As Group Finance & Operations Director, Mark has played a crucial role in guiding the Society through a challenging period of recovery, in the wake of the financial crisis, and into an exciting phase of growth. On behalf of the Board, I thank Mark for his outstanding contribution and wish him well in his retirement.

We welcomed our new Group Finance & Operations Director, Ashraf Piranie, in March 2017. In Ashraf, we have secured an individual of the highest calibre to succeed Mark. Ashraf comes to the West Brom from Nottingham Building Society where he held the positions of Deputy Chief Executive & Finance Director, playing an influential part in the Nottingham's growth and development. With over 20 years' experience in the financial services industry, Ashraf is a staunch advocate of the building society sector, and represents the Building Societies Association on the Prudential Regulation Authority's Practitioner Panel.

I am also delighted to welcome James Turner, who joined the Board as Non-Executive Director in April 2017. James brings a wealth of finance, audit and risk management experience. He is currently Director of Group Finance at Prudential plc.

Ashraf Piranie and James Turner will stand for election to the Board at the forthcoming Annual General Meeting.

Looking forward

Low interest rate prospects for the medium term are far from ideal for savers and we remain conscious of our responsibilities to support them whilst providing longstanding benefit to all of our members.

In this environment of global political and economic uncertainty, we will monitor developments very closely indeed. The Board is, however, satisfied that the Society has the capital and liquidity resources to continue fulfilling the needs of its membership and meeting its regulatory obligations. In January this year a third party challenged the eligibility of the Society's profit participating deferred shares (PPDS) for treatment as Common Equity Tier 1 (CET1), the highest quality of remunerated regulatory capital available to the Society. The Board, as announced on 7 February 2017, remains of the view that the PPDS, instruments developed in 2009 by the regulator at the time (the Financial Services Authority) and the Treasury, specifically to improve the quality of capital available to firms such as the West Brom, remain eligible as CET1. However, in the interests of certainty, the Society has approached the EBA for clarification. A response is awaited.

We believe firmly in the West Brom's strategy to return to core building society principles and will continue with our programmes of investing in core systems - to support excellent customer service - and responsibly managing down non-core portfolios.

I would like to express the Board's gratitude for the commitment and professionalism of the Society's staff and Executive team. Last, but by no means least, I sincerely thank our members for their continued support.

Mark Nicholls
Chairman
30 May 2017

Chief Executive's Review

I am proud to report a year of strong underlying performance and unwavering focus on our simple mutual philosophy – to provide members with a secure home for, and a good return on, their savings and the ability to realise their home ownership ambitions.

Performance overview

New prime residential mortgage lending totalled £712m (2015/16: £673m) and, overall, prime owner occupied loans grew by a further 15%, as new and existing customers were supported throughout the year with a competitive mortgage offering. Whilst our focus has been on growing the prime residential book, alongside this we have continued to reduce our exposure to commercial lending.

After adjustment for the one-off items explained below, underlying profitability improved markedly, up 60% from £4.8m to £7.7m.

60% increase
in underlying profit before tax
£4.8m 2015/16, up 60% to £7.7m

The statutory loss before tax of £19.8m (2015/16: profit of £13.5m) included the one-off costs of refunding additional interest charged since December 2013 on certain loans to landlord investors with multi-property portfolios. This followed the well-publicised overturning in June 2016, by the Court of Appeal, of an earlier decision of the High Court in respect of the Group's ability to vary the interest rate applicable to these loans. It is regrettable that our attempts to introduce fairness, for the benefit of our membership as a whole, were ultimately blocked. We have, nonetheless, duly met our obligations to cease charging the additional interest and to reimburse affected borrowers for what had previously been levied. The underlying profitability of £7.7m, referred to above, excludes the one-off costs of £27.5m. Of this amount, £8.7m related to additional interest charged on the affected loans during 2015/16 and has been adjusted for in the comparative figure.

£19.8m
Statutory loss before tax
2015/16 profit of £13.5m

The retail franchise remained strong, with retail deposits of £4.4bn (2015/16: £4.4bn) providing a healthy 104% (2015/16: 106%) cover for residential mortgage balances.

£4.4bn
Savings balances maintained
2015/16 £4.4bn

As capital is pivotal to the protection of members' interests it is pleasing that, despite reporting a loss and making significant investment in future growth, the Group's Common Equity Tier 1 (CET1) capital ratio remained robust at 13.8% (2015/16: 14.6%). At 6.8% (2015/16: 7.6%), our leverage ratio was one of the best in the bank and building society sector. As detailed in the Chairman's Statement, in January 2017, a third party alleged that the profit participating deferred shares (PPDS) of the Society do not comply with one aspect of the Capital Requirements Regulation criteria for eligibility as CET1. The Society's Board believes that the PPDS are eligible as CET1 and that the PPDS meet the CET1 criteria in all respects. The Board has sought external legal advice on this matter which has confirmed the Board's position. As explained, we now await a response from the European Banking Authority (EBA) in respect of the clarification we have sought on the matter. Should the EBA not agree our position, it is possible that we would have to reduce the degree to which the PPDS would count towards our CET1 by 50% immediately and thereafter by 10% per annum on each 1 January. Under this scenario, the immediate impact on our CET1 ratio would be a reduction from 13.8% at 31 March 2017 to 10.6%. The PPDS not included as CET1 would instead be included as Tier 2 capital so there would be no change to the total capital, or solvency, ratio of 16.0% as at that date and there would be no breach of any regulatory capital requirements.

13.8%
Common Equity Tier 1 Capital Ratio
14.6% 2015/16, down 0.8%

Asset quality

Residential mortgage arrears have fallen for the fourth consecutive year, evidencing the high credit quality of both new lending and the now well-seasoned back book. Since the Society's re-entry into the prime residential market, only one new customer has moved into a serious arrears position. At the year end, none remained in serious arrears.

The de-risking of the balance sheet has continued with a 14% decrease in our exposure to non-core commercial balances from £680m in 2015/16 to £588m. Some £73m of this exposure is in securitisation vehicles which have the effect of transferring the risk of loss out of the Society. Of the remaining £515m of exposure, £302m are non-performing loans being managed for recovery and £38m (7%) has been set aside as provisions in respect of these non-securitised commercial loans.

The Group's liquidity portfolio is efficiently managed and, at 31 March 2016 and 2017, all investment securities were rated single A or above or held with a Global Systemically Important Counterparty. The Society's Liquidity Coverage Ratio - a measure of whether there are sufficient high quality liquid assets to cover expected cash outflows under a 30-day liquidity stress scenario - was 127% (2015/16: 111%), comfortably in excess of the regulatory minimum.

Our members' needs

As a traditional, regional building society we remain committed to the principles of mutuality and all our decision-making is centred around the delivery of long-term value to our circa 446,000 members.

Help is always on hand in our branches to discuss borrowing and savings requirements.

The West Brom looks after the interests of its members by offering prime residential mortgages for homeowners, competitive retail savings and a range of ancillary products and services designed to meet individual financial needs. During the last financial year, we invested substantially in our mortgage application and customer management systems to make it easier for our members to do business with us and to provide operational efficiencies.

Throughout 2016/17 we offered borrowers a competitive range of fixed and discounted variable mortgages, including features such as fees assisted legal services, free valuations and cashbacks. These incentives were well received, in particular, by those borrowers looking to own their first home, with 23% of new mortgages advanced in the year attributable to first time buyers (2015/16: 21%).

23%

of new mortgages helping first time buyers
21% 2015/16, up 2%

Our mortgages were consistently featured in the Best Buy tables and, at the Consumer Moneyfacts Awards 2017, we were 'Highly Commended' in the category 'Remortgage Buyers' Choice'. During the year, the buildings and contents home insurance products, which complement our mortgage offering, each received the coveted Moneyfacts five star rating award.

Since 2012, the Society has worked with intermediaries to support its growth plans and enhance the accessibility of its mortgage products. Our high standards of service to mortgage brokers were recognised by the achievement of a top five star rating in the 2016 Financial Adviser Service Awards.

Savers faced further downward pressure on returns following the Monetary Policy Committee's decision to lower Bank Rate to 0.25% in August 2016 and of course the impact of the decision of the Court of Appeal I referred to earlier. Savings rates were also adversely impacted by the Bank of England's Term Funding Scheme, introduced to stimulate the mortgage markets by providing banks and building societies with low cost funding, which had the impact of lowering rates across the market. Despite this, the average interest margin paid to savers continues to remain above the average paid across the entire cash savings market.

Against this backdrop, the Society's net interest margin, which is broadly the difference between what is charged on mortgage lending and what is paid to savers, is not maximised but managed at a level which balances the current needs of savers and borrowers with the requirement to deliver business growth and member value over a longer horizon. Throughout the year, we maintained a consistent presence in the Best Buy tables, offering flexibility and choice through a range of savings products available via branch, post and online channels.

Acknowledging our members' aspirations to take control of their finances and plan for the future, the West Brom continues to partner with Wren Sterling, a leading national independent financial advisory business. Wren Sterling's expert advisers search the whole of the market for the right blend of products to meet members' needs and provide an ongoing relationship so that financial plans can be adapted to inevitable changes in personal circumstances.

We can facilitate independent financial advice for our members to help them plan for the future.

Our members' views

As a building society the West Brom operates first and foremost in the interests of its members.

Our expanding Customer Panel enables members to ultimately shape the way we do things. It provides a platform for us to engage with members and hear their views. During the year, we sought and responded to the Panel's feedback on topics such as our latest savings application form, communication preferences and what constitutes a great branch experience.

Members' ViewPoint events, hosted in the Head Office and in locations across the branch network, offer an opportunity for customers to make suggestions and convey their opinions about the Society to the Chief Executive and senior managers in a relaxed setting. This year, we discussed the future for interest rates, rewarding loyalty, mortgage fees and housing market growth with members who attended.

Real-time surveys within our Customer Services, Direct Mortgage and branch teams invite members to give immediate feedback on our service, an important tool for monitoring performance against members' expectations. During 2016/17, we were delighted to win 'Improvement Strategy of the Year' in the Midlands and Yorkshire Contact Centre Awards for improvements to our Customer Services department.

Our communities

We are proud of our mutual status and make a conscious effort to assist local communities, especially in the heartland area where our branches operate. This support can take a number of forms, starting with fundraising which we channel towards a different cause each year, as chosen by our colleagues.

Thumbs up for Stephen's Story and our chosen charity, Teenage Cancer Trust.

During the year, we worked with Teenage Cancer Trust, collecting more than £30,000 through a series of fundraising events and sponsored activities. The charity has a strong presence in the West Midlands through the specialist cancer support units it runs in local hospitals. We are pleased that the money we have raised will be spent in these specific areas, helping affected teenagers and their families cope with this most testing of diseases.

This year also marks the 10th anniversary of our partnership with Birmingham Children's Hospital and the launch of the Red Balloon Appeal Account, a savings product that generates funds for hospital projects. Since 2007 our customers have helped to raise a staggering £683,000 by choosing to save through the account, money which has been invested in everything from vital x-ray equipment to the creation of a centre dedicated to the treatment of rare diseases.

Support for worthy causes does not always have to be financial. We encourage colleagues to spend time volunteering in the local community and arrange regular projects that also serve to strengthen relationships between different business areas, departments and branch teams.

This extends to outreach work with schools and colleges where branch managers will regularly deliver financial awareness workshops themed around the true value of money, the cost of living and the dangers of excessive debt.

Pupils at ACE Academy in Tipton enjoyed discussing money management with staff from their local West Brom branch.

In recognition of our important work in the community, the West Brom was Highly Commended in the 2017 Mortgage Finance Gazette Award for Community Services.

Our people

The West Brom's reputation as a leading regional building society owes so much to the calibre of our people. The Investors in People Gold accreditation denotes an employer committed to attracting and retaining, through support and development opportunities, the very best talent.

2017 will see the launch of our Diversity Strategy which reinforces our pledge to recruit capable individuals from all backgrounds and ensure there are no barriers preventing any of our colleagues from maximising their potential. We were proud to be an early signatory to HM Treasury's Women in Finance Charter, which aims to improve the representation of women in senior managerial roles in financial services.

Conclusion and outlook

Interest rates are predicted to remain low for the coming year, maybe longer. Together with the availability of low cost funding through the Bank of England's Term Funding Scheme, this will stimulate lending but may also serve to intensify competition in the mortgage markets.

The Government's recent housing white paper, referred to in the Chairman's Statement, 'Fixing our Broken Housing Market', states an intention to increase the supply of new housing stock and provide affordable options for people wishing to buy or rent their own homes. We will keep abreast of these developments and consider any opportunities and concerns they present for home finance providers.

We will continue to invest in systems to improve the customer experience, as well as moving forwards with the Internal Ratings Based (IRB) approach to credit risk capital requirements - a regulatory project which we expect, due to the low risk nature of our core mortgage books, will ultimately improve our already robust capital position.

As the UK negotiates its departure from the EU, there is considerable uncertainty over its future relationships within and beyond Europe. Against this backdrop, we are starting to see a slowdown in house price inflation and real household income growth. While our prime residential mortgages are of a high credit quality and able to withstand a deterioration in market conditions, the commercial loan book is much more sensitive to adverse movements and further loss provisions may be necessary.

Despite the uncertainty that may result from the events of 2016, the Society has achieved lending growth and maintained a solid capital base. Furthermore, the upward trend in underlying profitability is testimony to the strength of the Society's business model. We are therefore well equipped to face the challenges which may lie ahead and remain confident in our ability to continue doing what we do best - fulfilling the needs of our membership.

It is, as always, my duty and privilege to thank our members for their enduring loyalty and also our people who work so tirelessly to earn it.

Jonathan Westhoff
Chief Executive
30 May 2017

Strategic Report

Our strategy

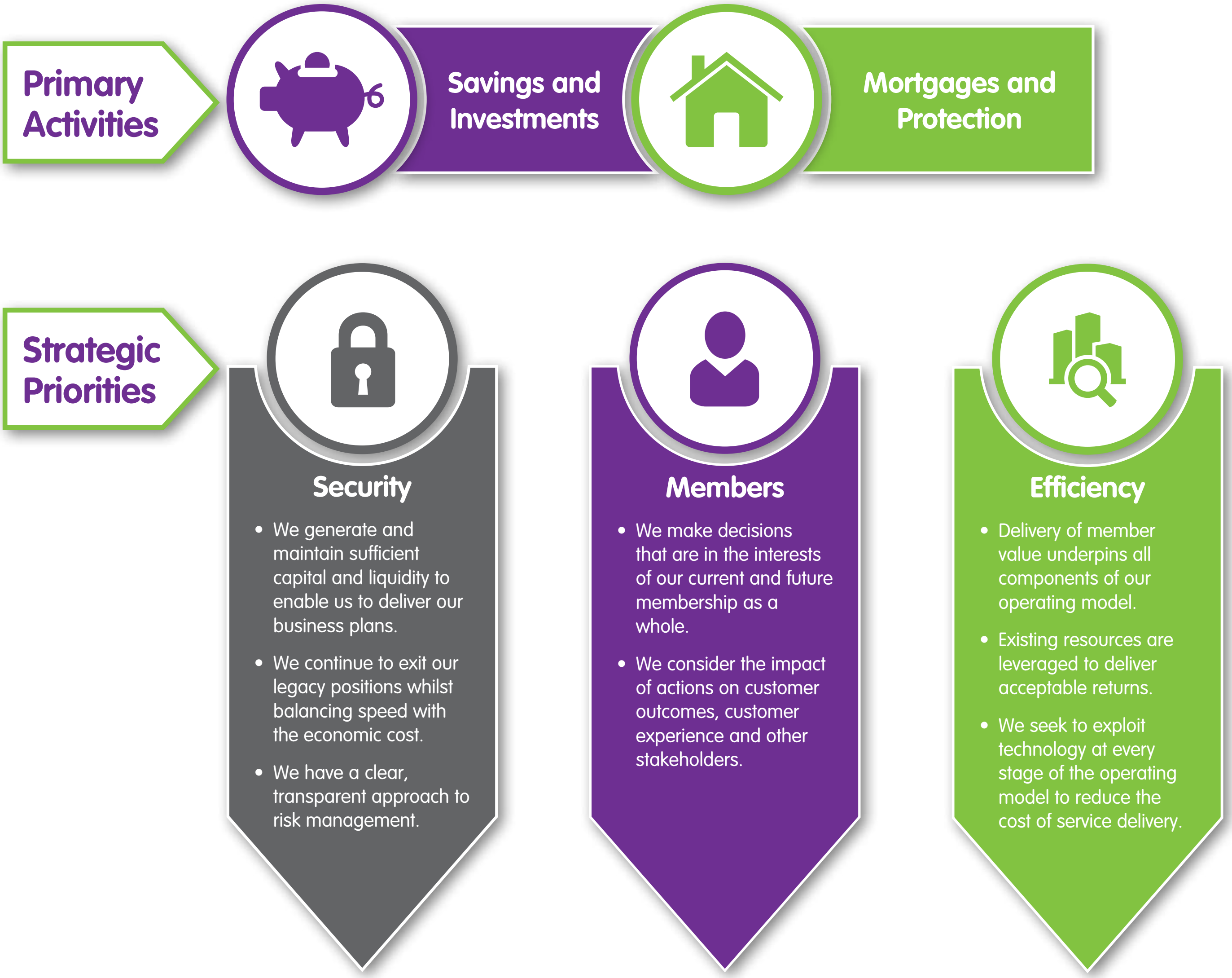
Following the financial crisis, we have pursued the strategy of taking the Society back to basics. Our strategy continues to focus on the simple premise of delivering our core purpose - supporting the financial wellbeing of our members by providing a safe and good return on the savings they entrust with us and promoting home ownership through responsible lending.

In delivering our savings and investments offering we aim to provide security, simplicity and value to our members. We strive to meet the needs of our members with a competitive range of products that offers transparency and clarity, delivering good returns. We continue to invest in our systems to make it easy for members to access our products and services.

The provision of residential mortgages is at the very heart of the mutual model. We understand the importance of a wide range of options for housing in the UK and our focus is primarily on the 'ownership' segment. Therefore we aim to provide cost effective ways to help our members achieve their ambitions.

Whilst we have made significant progress with our strategy over the last few years, we still have to manage down our non-core activities, in particular commercial lending. The Society will work to reduce its exposure to commercial mortgages, with new lending activity focused on owner occupied properties to good quality borrowers who can demonstrate their ability to meet their mortgage payments.

The business model employed to deliver the strategy is detailed below.



Our business model

The Society's strategic aims have resulted in a business model split between core and non-core activities. Our emphasis on the core activities of retail savings, investments and prime residential lending means that we are continuing to make a concerted effort to manage the orderly run-off of non-core activities.

The Group is organised into three main business segments:

Retail - residential lending, delivered through branch, direct and intermediary channels supported by retail savings products offered to customers through branch, internet and direct. Investments, general insurance and protection are either sold directly in our branches or in partnership with Wren Sterling. This segment also includes non-core second charge lending which is in run-off;

Commercial - the provision of finance for commercial real estate investment. This activity is considered non-core and inconsistent with the traditional building society model and is, therefore, being managed down; and

Property - a portfolio of residential properties held to generate rental income. During 2008, the Board concluded that it would not add any further investments and would, over time, respond to opportunities to dispose of properties where it was economically advantageous to do so. The portfolio is managed by Andrews Property Services, a well-respected property management company.

All of the above are supported by central functions which provide Finance, HR, IT, Compliance and Risk Management capabilities.

Funding is reviewed on a Group-wide level with the Treasury and Finance functions managing the day to day cash flows of the business, along with providing wholesale funding and ensuring the effective allocation of capital and liquidity.

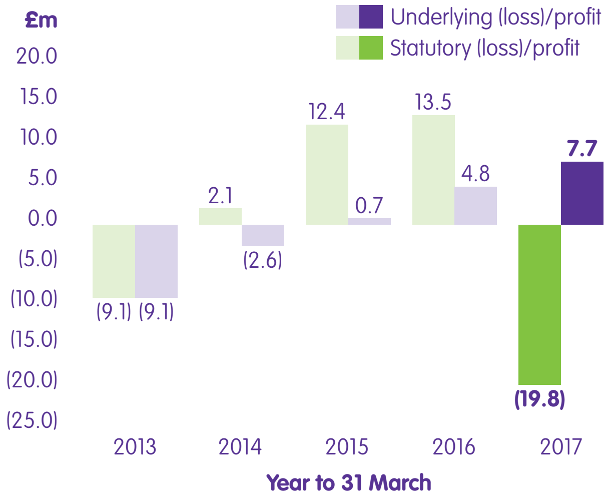
Key performance indicators

The Society monitors its progress against strategic objectives using a wide range of financial and non-financial key performance indicators (KPIs). The following sections of the Strategic Report clearly define these KPIs and describe the Society's performance against each.

Review of 2016/17

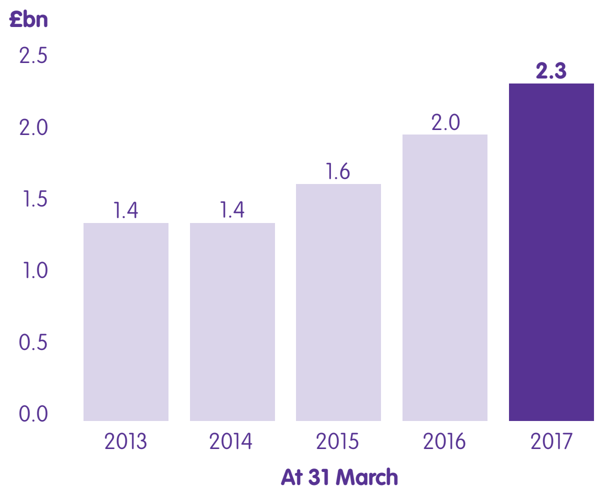
Pre-tax performance - The driver for reporting a statutory loss before tax of £19.8m (2015/16: profit of £13.5m) was the well-publicised reimbursement of interest on certain buy to let loans. Removing this one-off cost, the Group showed a strong underlying performance with underlying profit before tax up 60% to £7.7m (2015/16: £4.8m). Underlying net interest margin increased to 0.93% (2015/16: 0.90%).

(Loss)/Profit before tax



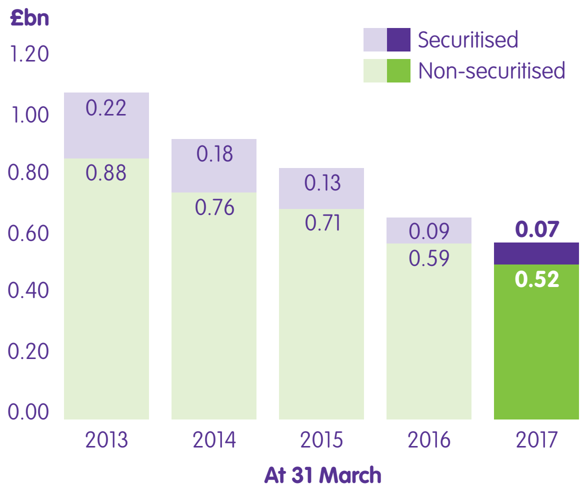
Lending - At £712m (2015/16: £673m), gross residential lending reached its highest level since the Society re-entered the mortgage market in 2012. Prime owner occupied mortgage balances grew for the fourth consecutive year, increasing by 15% to £2.3bn (2015/16: £2.0bn).

Prime owner occupied mortgage balances



Commercial mortgages - Non-core commercial mortgage balances fell 14% to £588m at 31 March 2017, advancing the strategy of de-risking the balance sheet.

Commercial lending balances*



*Commercial lending balances secured on commercial and residential property

Capital – Sound capital management practices have ensured that the Group's Common Equity Tier 1 ratio remains significantly in excess of regulatory requirements at 13.8% (2015/16: 14.6%). At 6.8% (2015/16: 7.6%), the leverage ratio was notably strong.

Performance overview

KEY performance indicators

The statutory and underlying results before tax are used to monitor the performance of the Group. The statutory result before tax is the most commonly used measure of profitability. However, where this includes one-off items that are not considered to reflect the continuing profitability of the Group, these items are excluded from underlying results to present a meaningful ongoing performance measure.

The Board assesses the Society's performance using the results before tax at both a total Group and individual business division level as this presents a more transparent view of the performance of the core and non-core elements of the Society.

Before one-off costs, underlying profitability improved significantly to £7.7m (2015/16: £4.8m). The non-recurring costs related to the Court of Appeal's overturning, in June 2016, of the High Court's previous decision about the Group's right to vary the interest rate on certain property investor loans. The outcome was that the Group ceased to levy the additional interest and refunded what had previously been charged, reporting the reimbursement under 'Provisions for liabilities' in the Income Statement. The estimated reduction in interest income for 2016/17, as a result of not receiving the additional rate, is £6.6m.

The table below gives a year on year comparison of underlying net interest income, net interest margin and profit before tax excluding the impact of the buy to let case:

Year to 31 March 2017 Underlying performance

	As reported £m	BTL case impact* £m	Underlying £m
Net interest income	**55.3**	**(1.2)**	**54.1**
(Loss)/Profit before tax	**(19.8)**	**27.5**	**7.7**
	%	**%**	**%**
Net interest margin	**0.95**	**(0.02)**	**0.93**

Year to 31 March 2016 Underlying performance

	As reported £m	BTL case impact* £m	Underlying £m
Net interest income	60.0	(8.7)	51.3
Profit before tax	13.5	(8.7)	4.8
	%	%	%
Net interest margin	1.06	(0.16)	0.90

*2016/17 included 2 months (2015/16: 12 months) of additional interest receivable which has been returned to borrowers following the overturning of the buy to let case. This has been deducted from net interest income in order to give a like-for-like comparison.

Overview by business division

Year to 31 March Underlying profit/(loss) before tax by division

	2017 £m	2016 £m
Retail	**10.6**	2.9
Commercial	**(9.3)**	(4.3)
Property	**6.4**	6.5
Intercompany adjustments	**-**	(0.3)
Total Group underlying profit before tax	**7.7**	4.8

Retail

The Retail segment's principal activities are residential mortgage lending and retail savings.

After removing the impact of the buy to let interest refund, Retail performance has markedly improved with an underlying profit before tax of £10.6m (2015/16: £2.9m). A 15% growth in prime residential mortgage balances, as a result of completions of £712m (2015/16: £673m), made a positive contribution to the segment result as did a £3.5m reduction (2015/16: £0.2m increase) in impairment provision requirements due to the high credit quality of the Society's core mortgage books.

Effective credit management kept arrears at a low level, with just 0.81% of residential mortgage accounts three months or more past due at the end of the year (2015/16: 1.27%).

Commercial

Commercial lending is a non-core activity and the Group continues to exit the market in a controlled manner so that losses are mitigated to the fullest extent possible.

Certain commercial property sectors do however remain volatile and, during the year, impairment charges rose to £11.1m, compared with £7.9m in 2015/16. This led to a decline in segment performance and an underlying loss before tax of £9.3m (2015/16: £4.3m).

The overall exposure to assets secured on commercial properties has fallen from £1.7bn in 2007/8 to £0.6bn at 31 March 2017. £73m of these balances are securitised (2015/16: £92m).

Property

The Property division, which is considered non-core, contributes to the results of the Group in two ways: rental income from the residential properties it holds and an increase in the market value of these properties.

A revaluation gain of £5.4m has been reported for the West Bromwich Homes Limited residential property portfolio (2015/16: £5.5m), as a result of house price inflation during the year. The carrying value of the portfolio at 31 March 2017 was £128.9m (2015/16: £123.7m). One property was sold during the year achieving its book value of £0.2m. Consistent with the prior period, the investment properties generated a trading net income of £1.0m.

Financial performance – Group

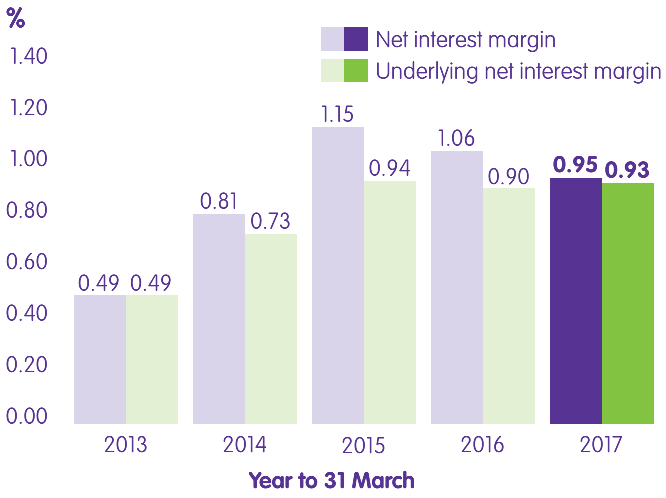
Net interest margin

KEY performance indicators

Net interest margin is calculated as net interest income expressed as a percentage of mean total assets.

The key drivers of this measure are the level of return received from the assets held by the Group and the interest paid on its borrowings. As the primary constituents of this measure are member related, being mortgages to borrowers and savings from retail customers, the Board's goal is not to maximise this ratio but to maintain a measured level that balances continued security with long-term value for the members.

Net interest margin



The net interest margin for the year ended 31 March 2017 was 0.95% (2015/16: 1.06%). Excluding the element of buy to let interest that has been refunded to customers, the underlying net interest margin increased slightly from 0.90% to 0.93%, partly attributable to the lower cost of funding following the introduction of the Bank of England's Term Funding Scheme (TFS) to promote UK lending growth.

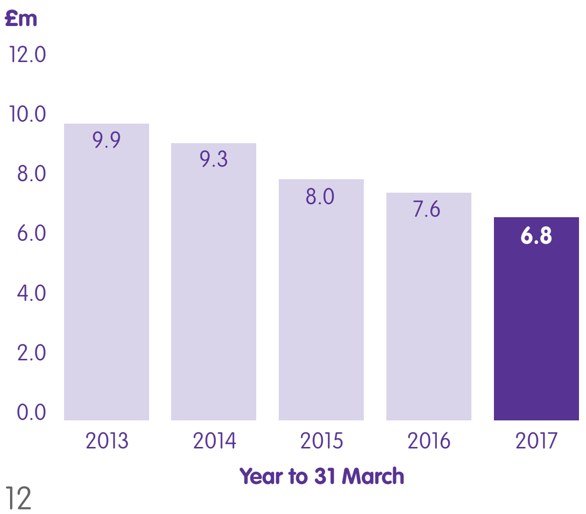
Notwithstanding the availability of low cost funding, the decrease in interest rates during the year has put some pressure on margins. As a mutual, it is not the West Brom's intention to maximise net interest margin but to maintain it at a level that delivers long-term value for members whilst continuing to provide them with a competitive product range.

Other income

KEY performance indicators

The Board monitors other income in absolute terms. Other income primarily represents income earned from the sale of non-margin related products. These include commission on the sale of insurance (in particular home and contents) and investment-related products, together with fees earned on lending and property rental activity.

Other income



Other income was £6.8m (2015/16: £7.6m), including £4.1m (2015/16: £4.1m) of investment property rental income generated by subsidiary West Bromwich Homes Limited.

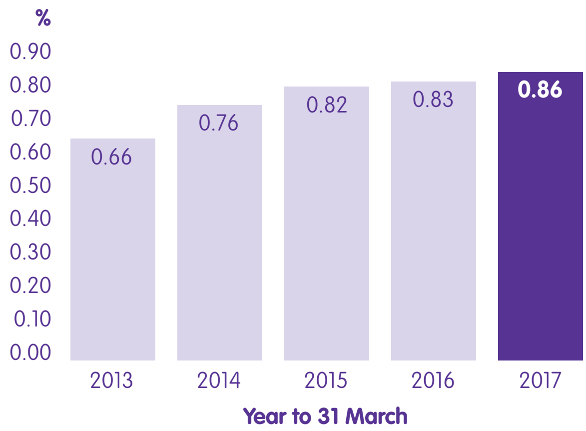
The remaining income stream is primarily derived from the Society's insurance, investment and protection product offering.

Management expenses

KEY performance indicators

The management expenses ratio is a measure of cost efficiency, reflecting costs as a proportion of total assets managed. It is calculated as total management expenses (including depreciation and amortisation) as a percentage of mean total assets.

Management expenses ratio



Management expenses were elevated in the year as the Society continued to invest in its infrastructure. The Head Office move was completed in April 2016, from which point the new building, fixtures and fittings became subject to depreciation charges which consequently increased from £5.1m to £5.7m for 2016/17.

During the year, the Society made further investment in core systems to enable growth and assure the ongoing provision of excellent customer service. Efficiency savings of circa £1m have been offset by the costs of resourcing a number of regulatory and technical projects, which require large teams with expertise in the relevant areas.

With inflation at 2.3%, the increase in administrative expenses from £42.0m to £44.4m was, in real terms, a 3.4% rise and the result of necessary investment, combined with the costs of regulatory compliance. The management expenses ratio for 2016/17 was 0.86% (2015/16: 0.83%).

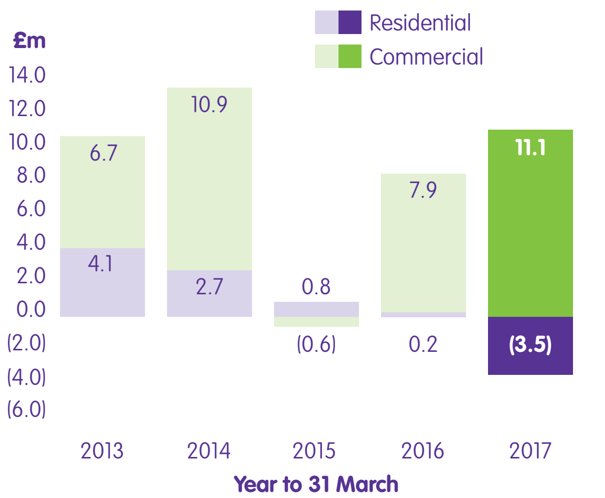
Impairment provisions on loans and advances

KEY performance indicators

The Board monitors the underlying level of impairment provisions, calculated as the absolute charge less offsetting fair value movements on derivatives used to hedge impaired loans. The indicator measures the credit risk performance of the assets (i.e. the lower the credit performance of the assets, the higher the losses). Provisions include the losses incurred or those losses expected to be incurred (based upon events that have already happened) and are calculated both individually and collectively on groups of assets with the same credit characteristics.

The key drivers of the quantum of losses incurred include unemployment, interest rates, movements in property prices, tenant defaults on commercial property and the availability of funding in the market.

Charge/(credit) for impairment losses on loans and advances



Since returning to the mortgage market in 2012/13, the Society has originated only prime residential loans. Historic balances are now well-seasoned. The high credit quality of the residential portfolios, together with the impact of house price inflation, has led to a £3.5m reversal of residential provision charges (2015/16: £0.2m increase).

At the year end date, the Group had £16.3m set aside for losses on residential mortgages (2015/16: £20.8m).

The Group has recognised commercial impairment charges of £11.1m in 2016/17 compared with £7.9m for the prior year. The increase reflected changes in circumstances for certain loans and is indicative of the vulnerability of the commercial property sector to fluctuating economic conditions.

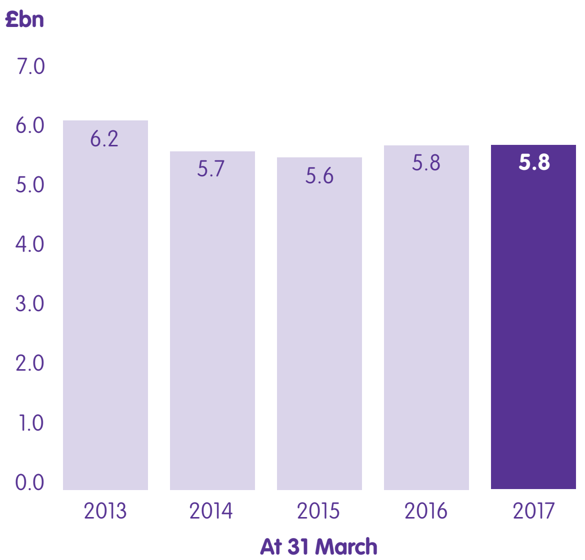
The commercial book is highly sensitive to any worsening in the economic climate and the Board remains committed to maintaining an appropriate level of cover against these non-core assets. Provisions held for commercial impairment were £39.4m at 31 March 2017 (2015/16: £43.9m), equivalent to 6.7% of the current loan book (2015/16: 6.5%).

A key strategy in mitigating the losses incurred on commercial loans is identifying circumstances whereby the appointment of a Law of Property Act Receiver (LPAR), to manage future cash flows, results in improved prospects of debt recovery. At 31 March 2017, 56% of commercial mortgage assets were LPAR-managed (2015/16: 46%).

Financial position

Total assets at the end of the year were maintained at £5.8bn, as lending growth offset the impact of running down non-core loan balances.

Group total assets



Loans and advances to customers

At £712m, residential mortgage advances were ahead of the comparative period (2015/16: £673m).

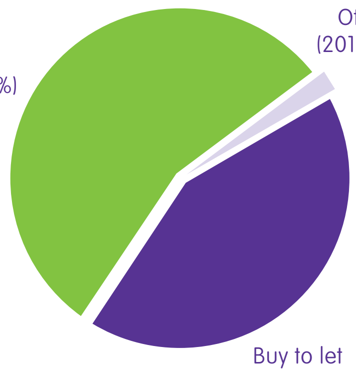
Throughout the year the West Brom has offered a range of competitive and Best Buy mortgage deals, including incentives such as free valuations and cashbacks, via its branch, direct and intermediary channels.

Residential lending

While all new lending is prime owner occupied, the Group's residential mortgage book also comprises buy to let mortgages and portfolios acquired through the Society's subsidiary company, West Bromwich Mortgage Company Limited. No buy to let lending has been carried out since 2009 and no portfolios have been acquired since 2005.

The composition of the residential mortgage portfolio at 31 March 2017 was 55.5% prime owner occupied (2015/16: 49.8%), 42.6% buy to let (2015/16: 48.0%) and 1.9% other (2015/16: 2.2%). The Society's new lending policies aim to rebalance the mortgage portfolio, increasing the proportion of the book made up of prime owner occupied loans.

Analysis by lending type at 31 March 2017



As illustrated in the analysis tables which follow, the regional spread of residential property assets is sufficiently diverse to mitigate geographical concentration risk. In line with expectation, the largest balances are in the West Midlands, being the Society's heartland, and the South East and Greater London, where property prices are highest.

At 31 March Residential loans analysis by region

	2017 %	2016 %
East Anglia	**2.9**	2.7
East Midlands	**9.8**	9.3
Greater London	**13.1**	14.4
Northern Ireland	**0.1**	0.1
North	**3.9**	3.6
North West	**11.7**	11.2
Scotland	**2.7**	3.1
South East	**17.7**	18.1
South West	**8.3**	8.2
Wales	**4.9**	4.7
West Midlands	**16.7**	17.3
Yorkshire	**8.2**	7.3
Total	**100.0**	100.0

KEY performance indicators

The Board reviews the credit performance of the Group's loans and receivables using a variety of measures that report on different characteristics and behaviours of both the loan and the customer. This is to ensure that all indicators of potential problems are identified as early as possible.

The principal industry standard and Board measure is the number of cases where the borrower has missed more than three monthly payments.

At 31 March 2017 Group arrears

	Total balances £m	**3 months+ %**
Prime owner occupied	**2,349.6**	**0.70**
Buy to let	**1,803.6**	**0.30**
Other	**63.6**	**6.81**
Core residential	**4,216.8**	**0.63**
Second charge lending	**18.3**	**8.58**
Total residential	**4,235.1**	**0.81**
Total residential including possessions	4,235.1	1.04

At 31 March 2016 Group arrears

	Total balances £m	3 months+ %
Prime owner occupied	2,045.6	0.96
Buy to let	1,974.7	0.90
Other	68.8	8.19
Core residential	4,089.1	1.07
Second charge lending	22.1	8.58
Total residential	4,111.2	1.27
Total residential including possessions	4,111.2	1.43

High quality lending, effective credit management practices and falling unemployment have all contributed to sustained low levels of arrears. At 31 March 2017, just 0.81% (2015/16: 1.27%) of accounts were three months or more in arrears. This compares favourably with data from the Council of Mortgage Lenders which showed that the average number of accounts greater than three months in arrears, as a percentage of total accounts, was 1.0% for the 2016 calendar year. Excluding the closed second charge lending portfolio, the residential arrears percentage was lower still at 0.63% (2015/16: 1.07%).

The Society engages in 'forbearance' to support borrowers experiencing genuine financial hardship and enable them to remain in their homes, where this action is not expected to increase the level of debt in the long term. Forbearance measures take a number of forms such as temporary reductions to contractual payments, interest capitalisation and term extensions. The Society's approach to forbearance is described in more detail in note 32 to the Accounts.

The Society's comprehensive pricing models and strict affordability criteria ensure that all new lending is undertaken within the Board's credit risk appetite.

Commercial

The commercial mortgage book is held within the Society's subsidiary company, West Bromwich Commercial Limited.

Board strategy is to exit this non-core business in a way that minimises losses, recognising that this may involve holding loans for an extended period, rather than initiating a quick and heavily discounted sale.

During the year, commercial mortgage balances fell 14% to £588m (2015/16: £680m) of which £73m is securitised (2015/16: £92m) with full provision made for the residual risk to the Group.

The table below analyses the commercial loan balances by industry type.

At 31 March Commercial loans

	2017 £m	2016 £m
Healthcare and leisure	**139.4**	167.0
Industrial and warehouse	**23.3**	23.1
Office	**35.1**	48.7
Retail	**305.4**	350.2
Residential property	**18.7**	20.2
Other	**21.3**	21.4
Fair value adjustments	**44.3**	49.0
Total	**587.5**	679.6

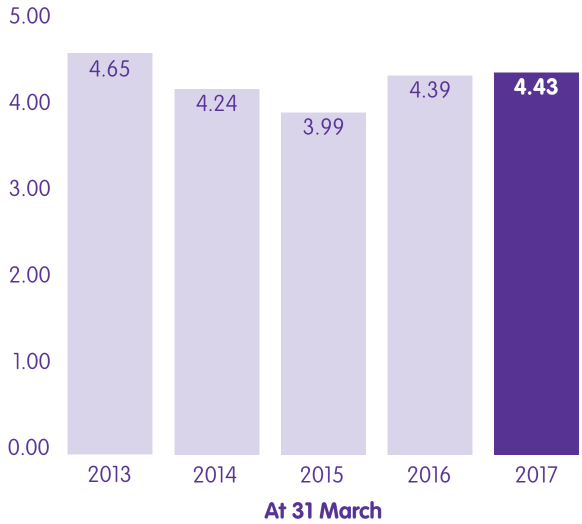
Funding

KEY performance indicators

The key funding measure that the Board uses to assess the risk in its funding base is the wholesale funding ratio. The wholesale funding ratio measures the proportion of total Society shares and borrowings (including non-recourse finance) not in the form of retail savings products. It assesses the Society's relative exposure to the wholesale funding markets and it is the Board's aim to maintain this ratio at a stable low level.

Retail

Aligned to the principles of mutuality, the Society is primarily funded by retail deposits, with residential mortgage assets amply covered 1.04 times (2015/16: 1.06 times) by retail savings balances.



The retail savings book marginally increased during the year to £4.43bn (2015/16: £4.39bn), with 60% (2015/16: 59%) held in branch-based accounts.

During the year, the Society has balanced its objective to offer competitive savings products with the need to efficiently manage levels of retail funding. Cash held in excess of that required for lending attracts minimal investment returns and therefore constrains overall profitability and member value.

Wholesale

At 31 March 2017, 16.0% of total shares and borrowings emanated from wholesale funding sources. The comparative wholesale funding ratio at 31 March 2016 was 15.2%.

Although the Society will remain predominantly funded by retail savings balances, the wholesale markets do offer some diversification and serve as a useful source of funding for the Society to access where it is economically effective to do so.

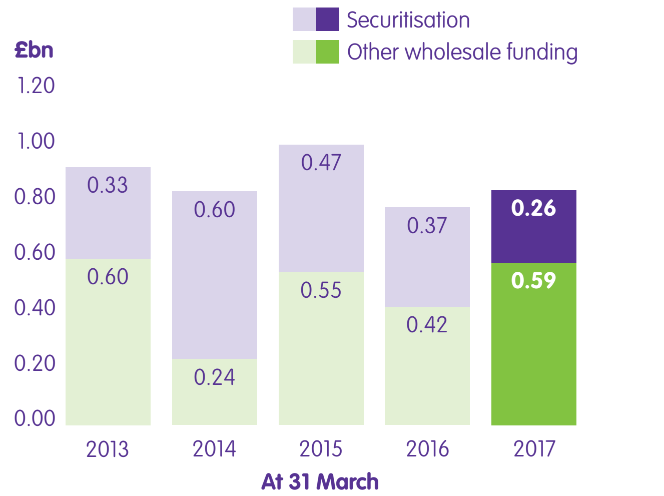
The Society's lending activities and high quality asset holdings provide access to the Bank of England's Term Funding Scheme (TFS). The West Brom, along with other financial institutions, has taken advantage of this opportunity to obtain low cost term funding.

The table below shows the high level composition of the wholesale funding portfolio.

At 31 March Wholesale funding sources

	2017 £m	2016 £m
Deposits	**583.0**	416.0
Securitisation	**263.2**	368.6
Total	**846.2**	784.6

Wholesale funding balances



Liquidity

KEY performance indicators

The Society's liquidity position is monitored in a number of different ways, including reviewing the components of its funding and liquidity portfolios, testing liquidity by selling into the market and monitoring the impact of a number of stressed scenarios. However, the key measures that the Board uses to monitor its liquidity position are:

- *Liquidity ratio - liquid assets as a proportion of shares and borrowings;*
- *'Buffer liquidity' - the most liquid and secure form of holding, comprising gilts, treasury bills, supranational bonds and reserves with the Bank of England. Buffer liquidity is assessed against limits set by the PRA and Board under the Liquidity Coverage Ratio regime;*
- *Liquidity Coverage Ratio (LCR) - high quality liquid assets as a proportion of stressed cash outflows over the next 30 days; and*
- *Net Stable Funding Ratio (NSFR) - the ratio of available stable funding to required stable funding, representing a longer term liquidity measure than the LCR.*

Liquidity management is key to ensuring the Society can fulfil its regulatory and operational obligations whilst controlling the cost of holding liquid assets.

At all times during the year, liquid asset balances exceeded regulatory limits and were maintained at levels sufficient to cover lending commitments and other cash outflows.

Liquid asset portfolios constitute low-risk investments; hence they typically generate very modest earnings relative to the cost of raising funds. To obviate the adverse financial impact of holding excess liquidity, the Society takes advantage of Bank of England schemes, available to the market, and other arrangements which provide 'off balance sheet' liquidity. These measures, which are subject to the provision of appropriate collateral, enable cash or liquid assets to be drawn down if required at a future date. At 31 March 2017, the Society held £57m of gilts, obtained under an asset swap agreement, which are not included in Group liquidity but do qualify as buffer liquidity for regulatory purposes (2015/16: £137m treasury bills obtained under the Funding for Lending Scheme).

Year end liquidity holdings comprise solely high quality liquid assets with 100% of treasury investments rated single A or better or held with a Global Systemically Important Counterparty (2015/16: 100%). The Group has no exposure to markets where concerns have been expressed, to non-UK sovereign debt or to any mortgage market outside the UK. There is no impairment provision requirement for treasury assets at 31 March 2017 (2015/16: nil).

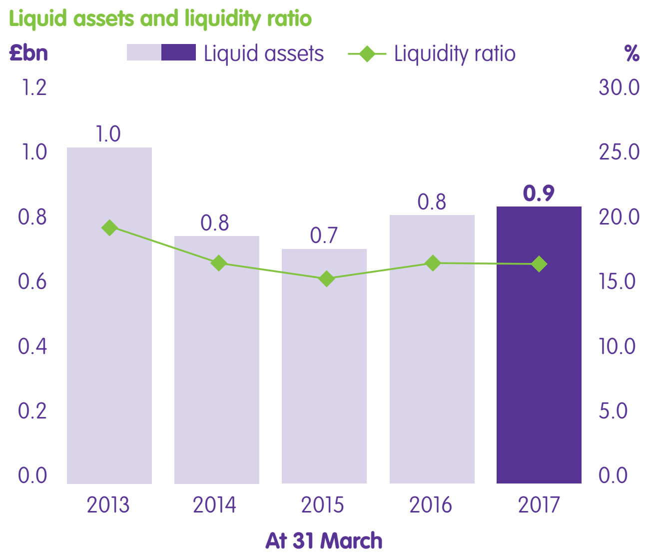
An analysis of the Group's liquidity portfolio is shown below.

At 31 March 2017 Liquidity portfolio

	£m	%
Buffer liquidity		
Cash and balances with the Bank of England	**287.6**	**33.7**
Supranationals	**89.7**	**10.5**
Covered bonds	**137.8**	**16.1**
Mortgage backed securities	**111.6**	**13.1**
Total buffer liquidity	**626.7**	**73.4**
Other securities - rated single A or better	**45.8**	**5.4**
Subsidiary/other liquidity	**181.3**	**21.2**
Total liquidity	**853.8**	**100.0**

At 31 March 2016 Liquidity portfolio

	£m	%
Buffer liquidity		
Cash and balances with the Bank of England	208.7	25.2
Supranationals	53.5	6.4
Covered bonds	124.0	14.9
Mortgage backed securities	109.4	13.2
Total buffer liquidity	495.6	59.7
Other securities - rated single A or better	123.2	14.9
Subsidiary/other liquidity	210.7	25.4
Total liquidity	829.5	100.0



Liquid asset balances were a little higher than the prior year at £854m (2015/16: £830m). The Society's 'on balance sheet' liquidity ratio was 17.0% (2015/16: 17.3%).

Under the CRD IV framework, the Prudential Regulation Authority (PRA) assesses liquidity using two metrics: the Liquidity Coverage Ratio (LCR) and Net Stable Funding Ratio (NSFR).

As at 31 March 2017, the Society's LCR ratio was 127% (2015/16: 111%) compared with a regulatory minimum of 100%.

The requirements for the NSFR are not yet finalised. The Society continues to monitor its NSFR position, based on current interpretation of the anticipated rules, and holds stable funding above the regulatory minimum of 100% which is expected to apply from 2018.

Capital

Capital is held as the ultimate protection for depositors. The Board sets the internal level of capital with the aim of ensuring capital levels are always above minimum regulatory requirements.

KEY performance indicators

Common Equity Tier 1 (CET1) capital is the strongest form of capital for any financial institution.

The primary indicator for monitoring capital is considered to be the CET1 ratio, calculated as CET1 capital divided by risk weighted assets.

In addition CRD IV has introduced the simpler non-risk based leverage ratio as a supplementary indicator. The leverage ratio is calculated as Tier 1 capital divided by total leverage ratio exposure. The relative simplicity of this measure is both a strength and a weakness. It removes the subjectivity associated with determining the risk weighting to be applied to each asset class, which can involve particularly complex models for the larger banks. In doing so, it effectively applies the same risk weighting to all asset classes when clearly the risks are not the same.

The table that follows includes both the Society's CET1 and leverage ratios. Figures have been quoted applying the current CRD IV transitional rules and also showing the full impact of CRD IV without the transitional rules.

At 31 March

	Notes	Transitional CRD IV rules 2017 £m	Full implementation of CRD IV 2017 £m	Transitional CRD IV rules 2016 £m	Full implementation of CRD IV 2016 £m
Common Equity Tier 1 capital					
General reserves		**211.0**	**211.0**	239.3	239.3
Revaluation reserve		**3.5**	**3.5**	3.4	3.4
Available for sale reserve (AFS)		**1.7**	**1.7**	0.9	0.9
Cash flow hedging reserve		**(0.7)**	**(0.7)**	(0.3)	(0.3)
Profit participating deferred shares		**173.0**	**173.0**	179.5	179.5
Common Equity Tier 1 prior to regulatory adjustments		**388.5**	**388.5**	422.8	422.8
Regulatory adjustments:					
Defined benefit pension fund asset	1	**-**	**-**	(0.8)	(0.8)
Cash flow hedging reserve	2	**0.7**	**0.7**	0.3	0.3
Intangible assets and goodwill	3	**(13.3)**	**(13.3)**	(8.2)	(8.2)
Deferred tax asset relating to operating losses	4	**(8.9)**	**(8.9)**	(14.7)	(14.7)
Other adjustments		**1.0**	**1.0**	(2.4)	(2.4)
Common Equity Tier 1 capital		**368.0**	**368.0**	397.0	397.0
Additional Tier 1 capital					
Permanent interest bearing shares (PIBS)		**75.0**	**75.0**	74.9	74.9
Regulatory adjustments:					
Amortisation of PIBS under transitional rules	5	**(37.5)**	**(75.0)**	(30.0)	(74.9)
Total Tier 1 capital		**405.5**	**368.0**	441.9	397.0
Tier 2 capital					
Collective provision		**22.1**	**22.1**	18.1	18.1
Contingency against collective provision add-back		**(2.5)**	**(2.5)**	-	-
Total capital		**425.1**	**387.6**	460.0	415.1
Risk weighted assets (RWA)					
Retail mortgages		**1,594.3**	**1,594.3**	1,570.5	1,570.5
Commercial loans		**654.4**	**654.4**	727.8	727.8
Treasury		**95.7**	**95.7**	120.7	120.7
Other		**176.1**	**176.1**	175.9	175.9
Market and counterparty credit risk		**47.8**	**47.8**	30.2	30.2
Operational risk		**95.9**	**95.9**	95.2	95.2
Total risk weighted assets		**2,664.2**	**2,664.2**	2,720.3	2,720.3
Total exposure for leverage ratio		**5,936.3**	**5,936.3**	5,789.2	5,789.2

		%	%	%	%
Common Equity Tier 1 (as a percentage of RWA)		**13.8**	**13.8**	14.6	14.6
Tier 1 (as a percentage of RWA)		**15.2**	**13.8**	16.2	14.6
Total capital (as a percentage of RWA)		**16.0**	**14.5**	16.9	15.3
Leverage ratio		**6.8**	**6.2**	7.6	6.9
Reconciliation of total assets as disclosed in the Statement of Financial Position to the leverage ratio exposures					
Total assets	6	**5,830.8**	**5,830.8**	5,767.1	5,767.1
Mortgage pipeline and committed facilities	7	**72.1**	**72.1**	79.7	79.7
Common Equity adjustments relating to assets	8	**(20.5)**	**(20.5)**	(26.1)	(26.1)
Netted derivative adjustment		**(37.9)**	**(37.9)**	(70.0)	(70.0)
Repurchase agreements and Potential Future Credit Exposure for swaps	9	**91.8**	**91.8**	38.5	38.5
Leverage ratio exposure		**5,936.3**	**5,936.3**	5,789.2	5,789.2

Notes

1. A full deduction is made from CET1 for the defined benefit pension fund asset.
2. The cash flow hedging reserve is not included in capital.
3. A full deduction is made from CET1 for intangible assets and goodwill.
4. Under the rules of CRD IV (transitional and on full implementation) deferred tax assets relating to previous operating losses are deducted from capital.
5. Under the transitional rules applicable to the current year, 50% of the value of PIBS is deducted from Tier 1 capital. Under the transitional rules the amortisation deduction is increased by 10% p.a. every 1 January through to 2021, with the final 10% deducted on 5 April 2021, the earliest call date for the PIBS.
6. The leverage ratio is based on total assets including all structured entities.
7. A 50% weighting is applied to mortgage pipeline and committed facilities assuming that in practice these retail commitments will not be cancelled.
8. The regulatory adjustments above include deductions relating to other assets which are also deducted from the total assets in the leverage calculation.
9. Repurchase agreements represent the extent to which collateral provided on repurchase agreements exceeds the amount borrowed.

The statutory loss for the financial year caused a reduction in the CET1 capital ratio which fell to 13.8% (2015/16: 14.6%). Notwithstanding this downwards movement, the CET1 ratio remains comfortably in excess of regulatory requirements and testament to the Society's financial resilience.

At 6.8%, (2015/16: 7.6%) the Society's leverage ratio remains exceptionally strong.

It should be noted that the Society issued an announcement on 7 February 2017 to confirm its regulatory capital position.

The Society is required to hold a certain amount of Common Equity Tier 1 (CET1) as part of its regulatory capital. For the Society, CET1 capital includes profit participating deferred shares (PPDS). The PPDS need to comply with certain criteria in order to qualify as CET1 as a matter of law (the CET1 Criteria). A third party has alleged that the PPDS of the Society do not comply with one aspect of the CET1 Criteria. If this were to be correct, the Society would, over time, need to reduce the degree to which the PPDS count towards its CET1 capital, with the PPDS not included as CET1 included instead as Tier 2 capital.

The Society's Board believes that the PPDS are eligible as CET1 and that the PPDS meet the CET1 Criteria in all respects. The Board has sought external legal advice on this matter which has confirmed the Board's position. The Society has agreed with its regulator, the Prudential Regulation Authority (PRA), that it is appropriate to continue to treat PPDS as CET1. However, in the interests of certainty, the Society has sought and currently awaits clarification from the European Banking Authority (EBA) on this matter.

Until such confirmation is obtained from the EBA, the Board believes that it will be prudent to manage the Society so that it is protected from the possibility of an unexpected outcome. To this end, the Society will be considering its options to help guard against the possibility of the EBA deciding that the PPDS do not comply with the CET1 Criteria and will seek to engage as appropriate with PPDS holders.

Were the EBA to determine that the PPDS do not meet the CET1 Criteria and the Society has not reached agreement with the holders of the PPDS, it is possible that the Society would have to reduce the degree to which the PPDS would count towards its CET1 by 50% immediately and thereafter by 10% per annum on each 1 January. Under this scenario, the immediate impact on the Society's CET1 ratio would be a reduction from 13.8% at 31 March 2017 to 10.6%. The total capital ratio of the Society would be unchanged at 16.0% as at that date because, as explained above, the element of PPDS that would be deemed not to qualify for CET1 would instead qualify for Tier 2 capital.

This would not result in the Society breaching any capital regulatory requirements set by the PRA. However, as the effect of the PPDS being deemed not to comply with the CET1 Criteria would mean the level of CET1 would reduce over time, the Board considers it important to explore options to ensure sound prudential planning and put the Society in a position to maintain healthy levels of CET1 for the foreseeable future under all outcomes.

Member engagement

At the West Brom we conduct regular research to understand how well we are meeting the financial needs, interests and expectations of our membership. The Board also monitors the feedback we receive from members so that improvements can be made to the broad range of products and services we offer.

KEY performance indicators

The Board reviews a range of customer research programmes, with the key ones being:

- *Mystery Shopper - conducted across our branch network. Mystery shoppers record their experiences against the standards that we expect our members to receive;*
- *Real-time surveys - members contacting our Customer Services and Retail Mortgage teams or visiting their local branch are asked to score the quality of service received and suggest ways in which we could improve;*
- *Postal and email surveys - we send our members short surveys by post or email on a variety of subjects, e.g. following a recent product purchase;*
- *Members' ViewPoint - events which seek face-to-face feedback from members and are held twice-yearly; and*
- *Customer Panel - made up of mortgage and savings customers who respond to online questionnaires about Society products and their opinions on money matters in general.*

Our Mystery Shopper programme is an ongoing quarterly measure of how branches are performing against agreed service standards which our members expect to receive. These visits are conducted by an independent specialist rather than Society personnel and captured using the latest digital video recording technology. Their findings help to coach colleagues in customer facing roles on best practice techniques.

Members' ViewPoint events are held regularly to capture thoughts and opinions from our customers.

The real-time survey enables us to record feedback in the moment and instantly log a satisfaction score while the experience is still fresh in the customer's mind. Both existing and potential customers are invited to take part in a short survey within minutes of making an enquiry or completing a transaction. As well as rating the West Brom, they can offer suggestions for how we might make things better. Since comments are monitored in real-time, any praise can be quickly passed on and any issues or concerns resolved directly with the customer. Satisfaction scores during the year remained consistently high across all channels, ending the year at an average of 9.34 out of 10.

For more detailed insight into a customer's full experience of using the West Brom, we carry out post-completion surveys either through the mail with paper-based responses or electronically via the internet. An example of this approach in action is with new mortgage borrowers, who are asked questions about the service received from the application process through to completion. Our scores have steadily improved over recent years from 4.1 out of 5 in 2014/15, when we first began issuing surveys to mortgage customers, to 4.4 in 2016/17.

We value face-to-face feedback enormously and host events where customers can openly convey their impressions of the Society to the Chief Executive and other senior executives. Called Members' ViewPoint, we run at least two sessions every year at different locations across our branch network. In 2016/17, we took the opportunity to also host a ViewPoint event at the Society's new head office premises at Providence Place in West Bromwich so that customers could see behind the scenes and learn more about the improved facilities.

A total of 2,369 members have joined our Customer Panel since it was introduced in 2014 as a way of offering feedback on our products and services. Operated digitally via email and the internet, we invite panel members to complete regular questionnaires, user-test new promotional literature and share their thoughts on pertinent sector issues such as savings habits, interest rates and the housing market.

Corporate and social responsibility

Social and community impact

It is part of our mutual ethos to show support for the local communities in which we operate. Our people strive to make contributions to those facing hardship and disadvantage through a variety of methods.

- **Financial aid**
  The Society makes grant funding available to a variety of small charities and community groups through the Mercian Community Trust. Money is sourced through our Community Account, an affinity savings product, and then distributed in partnership with the Diocese of Lichfield. Beneficiaries are associated with issues such as ill health, social wellbeing, disability, vulnerability, bereavement and domestic violence. We ask that charities are active within our heartland area and contributions range from a few hundred pounds to several thousand. We welcome approaches from the charities themselves, but find it particularly satisfying when colleagues and customers make suggestions for grants. This happened recently with our Walsall branch, where a customer asked the Trust to consider supporting St Giles Hospice because of the care they showed his late mother. This resulted in a £5,000 donation to invest in care facilities.

- **Fundraising**
  West Brom colleagues are always enthusiastic and creative when it comes to developing fundraising ideas for our charity of the year. Playing a part in the selection of this charity partner, which we do through an annual vote, helps to boost engagement levels and this was clear to see in our most recent experience with Teenage Cancer Trust. While operating nationally, our partnership focused on the Trust's support network in the West Midlands Region, which involves the running of specialist cancer units at Birmingham Children's Hospital, Queen Elizabeth Hospital Birmingham and the Royal Orthopaedic Hospital in Northfield. From golf days and football tournaments, to cake bakes and sponsored walks, our fundraising efforts have generated more than £30,000 to help cancer patients and their families.

A busy programme of fundraising events each year helps to raise money for our chosen charity.

- **Affinity partnerships**
  Our customers are invited to save with the Society through a number of special affinity accounts which see a proportion of savings interest diverted to different causes. This creates an annual bonus for the affinity partner, be that a charity as in the case of Birmingham Children's Hospital, or a sporting club such as West Bromwich Albion or Walsall FC.

- **Volunteering programme**
  Colleagues can spend up to two days each year carrying out voluntary work and around 60 took up the opportunity to do so during the past year. Notable projects included tree planting and conservation work in the grounds of Queen Elizabeth Hospital Birmingham and painting and decorating at Roshni, a women's refuge in Handsworth. Groups of volunteers also visited local hospitals during the Christmas period to brighten up the children's wards with festive decorations. Our 'Money-Go-Round' workshops continue to be popular in local schools, where branch managers spend time talking about financial awareness and the importance of good money management from an early age. We estimate some 3,000 children have participated to date.

Society volunteers stepped in to help spruce up the facilities at women's refuge Roshni.

Employee diversity

The West Brom values people from all backgrounds and recognises the importance of diversity and inclusion. We operate from one of the most ethnically diverse regions in the country, which is reflected in the composition of our workforce with over a quarter, 27%, drawn from ethnic minority communities.
This representation supports our ambition to deliver outstanding service given that many of our branches serve a mixed ethnic population. Many staff members are multilingual and can therefore converse with customers where English is not their first language.

With a total staff number of 742 as at 31 March 2017, female colleagues amount to 451, some 61% of the overall figure. Of the Society's Retail and Branch management team, 57% are female and, at a senior managerial level, the proportion is 38 male managers to 12 female managers. We have increased diversity on our Board, with a second female Non-Executive Director appointed during the year.

Our commitment is to create a culture where colleagues feel they can share our values, fulfil their potential and be appropriately rewarded irrespective of their background. In order to meet this commitment, we are developing a Diversity Strategy to be launched later this year. As part of this initiative, the Society has signed up to the Women in Finance Charter and set two targets for female representation to be achieved by 2020. These are to increase female representation at Board level to 30% and for 30% of the senior management population to be female.

Taxation

The statutory reported tax charge for the year is £6.0m (2015/16: £4.1m) due mainly to the write down of the deferred tax asset, in relation to brought forward losses, to a level expected to be recoverable in the next five years. The estimated recoverable amount reduced following the outcome of the legal case which affected the Group's ability to vary the interest rate applicable to certain buy to let loans.

Total tax contribution

During 2016/17 the Group incurred taxes of £5.9m (2015/16: £9.5m) including £3.7m (2015/16: £7.4m) of irrecoverable VAT, which represents a cost to the Group reported within administrative expenses and depreciation.

Year to 31 March

	2017 £m	2016 £m
Taxes paid		
Indirect taxes (irrecoverable VAT)	**3.7**	7.4
Employment taxes (Employer's NI)	**2.2**	2.1
Total	**5.9**	9.5

In addition, the Group collected and remitted, on behalf of HM Revenue & Customs, a further £11.0m (2015/16: £14.5m) as shown in the table below.

Year to 31 March

	2017 £m	2016 £m
Taxes collected and remitted		
Taxes withheld at source	**2.9**	6.9
Payroll taxes (PAYE and Employees' NI)	**8.0**	7.5
Indirect taxes (Insurance Premium Tax and VAT)	**0.1**	0.1
Total	**11.0**	14.5

Taxes collected and remitted on behalf of HM Revenue & Customs fell following the introduction of the new personal savings allowance, which means that banks and building societies no longer deduct tax from the interest paid on savings.

Principal risks and uncertainties

Effective risk management is integral to the Society's operations.

The separate Risk Management Report on pages 23 to 27 identifies the principal risks and uncertainties faced by the Society and describes, in detail, the West Brom's approach to risk management.

Outlook

The West Brom's strategy is to conform to the mutual model in its purest sense - enabling home ownership by providing residential mortgages which are predominantly funded by retail deposits.

In anticipation of a prolonged period of low interest rates, we will endeavour to balance the needs of our saving and borrowing members, whilst securing long-term member value by growing our capital base. The derisking of the balance sheet is integral to the Board's strategy and the managed exit from non-core activities is set to continue in 2017/18.

In a time of extraordinary political turbulence, most poignantly in respect of the UK's departure from the EU, future market movements are difficult to predict. We do, however, take confidence from our strong capital and liquidity positions which we regularly test against a number of stressed scenarios. The new accounting standard, IFRS 9 Financial Instruments, which the Society must apply from 1 April 2018, is more forward-looking than its predecessor, IAS 39, and incorporates a number of alternative economic outcomes in the calculation of expected credit losses. Over the coming year, we will continue to consider the capital impact of implementation for both the residential and more market-sensitive commercial books.

The Term Funding Scheme (TFS) launched in 2016/17 will make inexpensive funding available for the forthcoming financial year. Use of the TFS will support the Society's plans for lending growth and further strategic investment, which is necessary to improve access to our products and to maintain first-rate customer service standards. The mortgage markets are, however, expected to remain highly competitive in response to the Bank of England stimulus.

In summary, while the economic repercussions of Brexit and worldwide political changes are not yet known, the Society is well positioned to adhere to its overarching mutual principles and to move forward with its plans for steady growth.

Ashraf Piranie
Group Finance & Operations Director
30 May 2017

Risk Management

Overview

Effective management of risks and opportunities is essential to achieving the Society's objectives. The Board aims to manage effectively all the risks that arise from its activities and believes that its approach to risk management reflects an understanding of actual and potential risk exposures, the quantification of the impact of such exposures and the development and implementation of controls that manage exposures within the Board's agreed risk appetite.

Risk management framework

The Society's activities are governed by its constitution, principles and values. The Directors have also agreed a set of statements which describe the Board's risk appetite in terms of a number of principal key risk categories: business, credit, capital, liquidity, market, basis, operational, retail conduct, pension liability and information (the Society's Risk Appetite Statements).

These Risk Appetite Statements drive corporate planning activity, including capital and liquidity planning, as well as providing the basis for key risk measures.

The final element of the framework is the formal structure for managing risk across the Group. This is based on the 'Three Lines of Defence' model which is illustrated below.

	Activity	Responsibility	Governance
1st	Business Operations	Line Management	Line Management Oversight
2nd	Policy, Controls, Measure, Monitor	Control Functions	Management and Board Committees
3rd	Assurance	Internal Audit	Audit Committee

Governance structure

During the year, risk governance was provided by a structure consisting of nine key risk management committees:

Risk Committee (RC) - Comprising of all of the Non-Executive Directors except the Chairman, this Committee is responsible for the oversight and management of the principal and key strategic risks identified by the Board.

Executive Risk Committee (ERC) - This Committee is chaired by the Chief Financial Risk Officer and is responsible for providing the Executive and the Risk Committee with an enterprise wide view of the risk profile of the Society, including current and potential risks. The ERC is also accountable for driving the detailed implementation of the Society's Risk Management Framework.

Assets & Liabilities Committee (ALCo) - This Committee is chaired by the Group Finance & Operations Director and is responsible for overseeing the assets and liabilities risk including the assessment of exposure to Treasury counterparty credit, market, liquidity, pension liability, basis and interest rate risk.

Residential Credit Committee (RCC) - This Committee is chaired by the Chief Financial Risk Officer and is responsible for monitoring the Society's residential lending activity and its exposure to credit risks in the retail loan books.

Commercial Loans Risk Committee (CLRC) - This Committee is chaired by the Chief Financial Risk Officer and is responsible for monitoring the Society's exposure to credit risks in the commercial loan book.

Operational and Conduct Risk Group (OCRG) - This Group is chaired by the Group Secretary and is responsible for the oversight of the management of operational and retail conduct risks arising from the Society's business activities.

Information Risk Group (IRG) - This Group is chaired by the Group Secretary and is in place to maintain oversight and governance of information risk across the Society and challenge the effectiveness of the controls in place to mitigate information risk (including cyber security). Its purpose is to support and drive the information risk governance agenda and provide oversight that effective information governance best practice mechanisms are in place within the Society.

Group Capital Committee (GCC) - This Committee is chaired by the Group Finance & Operations Director and is responsible for reviewing the Group's capital requirements.

Audit Committee (AC) - Comprising four Non-Executive Directors, the Audit Committee provides the Board with assurance regarding the integrity of the financial statements and the adequacy and effectiveness of the Society's risk management frameworks.

Independent assurance is provided by the Internal Audit function which has a direct reporting line into the Audit Committee.

Risk categories

The Board has identified ten principal risk categories, which together define its overall risk universe. These are defined below:

Business risk

The risk of the Society failing to meet its business objectives through the inappropriate selection or implementation of strategic plans.

Credit risk

The risk that losses may arise as a result of the Society's borrowers, debtors or market counterparties failing to meet their obligations to repay.

Capital risk

The risk that the Society has insufficient capital to cover stressed losses or to meet regulatory requirements.

Liquidity risk

The risk that the Society either does not have sufficient financial resources to enable it to meet its obligations as they fall due or can secure such resources only at excessive cost.

Market risk

The risk of changes in the value of, or income arising from, the Society's assets and liabilities as a result of unexpected changes in financial prices, primarily interest rates, property prices, bond yields and inflation.

Basis risk

The risk of divergence in interest rates for different balance sheet elements and that it may not be possible to decrease/increase administered savings rates in line with decreases/increases in money market (LIBOR) rates, resulting in a margin squeeze where lending is LIBOR-based.

Operational risk
The risk of loss and/or negative impact to the Society resulting from inadequate or failed internal processes, systems or people, or from external events.

Retail conduct risk
The risk that inappropriate behaviours by the Society result in adverse outcomes for retail consumers.

Pension liability risk
The risk that there will be a shortfall in the value of the Society's pension fund assets over and above the guaranteed liability to its employees under the defined benefit pension scheme. This may result from a number of sources including investment strategy, investment performance, market factors and mortality rates.

Information risk
The risk that customer or Society information assets are managed or processed incorrectly or are not adequately protected. It includes inadequate data quality and failure to comply with data protection and data privacy requirements.

For each risk category the Board has agreed an appetite statement and key metrics which, together, define the level of risk the Board is prepared to accept or tolerate. In addition, key threats and the corresponding Society responses or mitigants, as well as opportunities, have been identified. The mitigating controls and the effectiveness of the controls are monitored by line management, with control functions providing a Second Line of Defence. Internal Audit, through an approved assurance programme, provides the Third Line of Defence.

The Risk Committee meets at least quarterly to review the Society's exposure to the risk categories. During this financial year, the Committee met on nine occasions.

Business conditions and the economic environment
Notwithstanding the Brexit vote, the UK economy has continued to perform well. The Bank of England lowered interest rates further to a new record and increased quantitative easing that injects money into the economy to offset any potential adverse impact of Brexit. The strength of the economy continues to be driven by household consumption and consumer confidence remained high during 2016. UK inflation is starting to edge higher following the fall in sterling but the continuing low cost of borrowing supports improving customer affordability and has driven the growth of consumer debt to record levels.

The cost of retail mortgages has continued to fall, driven by increasing competition in the market and a greater focus on lending to owner-occupiers, given the macroprudential and fiscal policy changes announced to impact the buy to let market in 2016.

The West Brom is exclusively focused in the UK and, therefore, the general UK macro-economic environment is key to its success. It is anticipated that post triggering of Article 50, the Brexit negotiations will potentially introduce some economic uncertainty that may impact consumer confidence.

The external factors that impact the Society include:

- Interest rates (Bank Rate and LIBOR);
- Inflation;
- Unemployment; and
- The housing and commercial property markets.

Day-to-day management of key risks
Primary responsibility for risk management, including the design and operation of effective controls, rests with the management of each business function - the 'First Line of Defence'. Support and challenge is provided through specialist risk functions - Credit Risk, Operational Risk, Conduct Risk and Assets & Liabilities Management - the 'Second Line of Defence'. These functions develop and review policies, monitor and support compliance with those policies, and support the business functions to manage risk.

Governance and oversight is provided through a number of management and executive committees as detailed on page 23.

Credit risk
Credit risk refers to the risk that a customer or counterparty to a contract will not be able to meet their obligations as they fall due. For the purposes of the Society, this normally means the risk that a borrower will not repay their mortgage loan, or that a financial institution will not repay funds invested by the Society in that institution.

During the year the Society's lending was in accordance with the approved credit policy, which is consistent with the risk appetite established by the Board. Currently, no new non-conforming property lending (i.e. commercial, buy to let, sub-prime or self-certified) is being undertaken.

The Society's exposure to residential and commercial credit risk is managed by a specialist Credit Risk team which is responsible for setting the Credit Risk Management Framework and associated limits. It also provides regular reports to the Risk Committee, which is chaired by a Non-Executive Director and includes all other Non-Executive Directors, except the Chairman, as members.

Additionally, credit risk can arise within treasury transactions (used to meet liquidity requirements and those hedging instruments used for interest rate risk purposes). This type of credit risk is managed by the Treasury Middle Office team. On a daily basis, this team monitors exposures to counterparties and countries, and ensures operations remain within Board approved limits. ALCo and the Board review the Treasury Policy and limits, with reports presented to ALCo on a monthly basis confirming compliance with such policy limits.

Throughout the last financial year, a conservative approach to liquidity management has been maintained, investing for short periods with selected financial institutions. The Society has also maintained a position of holding a significant proportion of liquidity in UK government guaranteed and supranational financial institution assets, which are considered to be both highly liquid and secure. Treasury operates a strict control framework and exposures are monitored on a daily basis.

Market risk
Market risk refers to the possible changes in the value of, or

income arising from, the Society's assets and liabilities as a result of changes in interest/exchange rates, property prices or equities. Market risk exposures are managed through the Treasury department which is responsible for managing exposure to all aspects of market risk within parameters set by the Board.

ALCo reviews the Treasury Policy, recommending changes to the Board as appropriate, and ensures that regular reports on all aspects of market risk are assessed and reported to the Board. The key market risk is interest rate risk, which arises as a result of differences in the timing of interest rate re-pricing of assets and liabilities. To mitigate this, Treasury uses natural balance sheet hedging (e.g. matching 2 year fixed rate mortgages with 2 year fixed rate saving bonds) and derivative instruments. The use of derivatives is only permitted in accordance with the provisions of the Building Societies Act 1986, which focus on their use to reduce risk.

The maximum level of interest rate risk is governed by the Board approved Treasury Policy in line with the Board's risk appetite.

In line with regulatory requirements and best practice, the impact of a parallel shift in interest rates in both directions, is considered. In addition, the impact of alternative non-parallel scenarios upon income and market value is also considered.

Interest rate sensitivity also arises from the potential for different interest rates to move in different ways, e.g. Bank Rate mortgages are funded by LIBOR-linked liabilities. The impact of these mismatches (basis risk) is monitored by Treasury and reported to ALCo.

The Society's main exposure to equities is through the defined benefit pension scheme. While the Society does attract funds through index-linked savings products, all exposures to equity indices are fully hedged. There is no exposure to foreign exchange rates.

The Society has invested in property through its subsidiary West Bromwich Homes Limited and offers residential property for rent. This non-core business exposes the Society to movements in house prices. The Board's strategy is to exit from this business when market conditions are opportune.

Liquidity risk

The Society's primary purpose is to make loans secured by way of mortgage on residential property. It funds these loans substantially from short term deposits provided by its saving members. The contractual maturity of the mortgages is typically up to 25 years although loans are often repaid early due to borrowers moving house or remortgaging.

Savers' deposits, whilst accessible predominantly on demand, at short notice or for fixed periods, nevertheless tend to remain with the Society for longer periods. A substantial proportion of savers have long established relationships with the Society.

This difference in the nature of borrowers' and savers' relationships causes a structural mismatch between the speed at which the Group can generate cash from its business assets and the demand for funds to meet its liabilities. To mitigate this risk, the Group holds sufficient liquid resources to meet the normal day-to-day operations of the business and, in addition, maintains a buffer of high quality liquid assets which can be converted quickly into cash to cover outflows in severely stressed conditions. Processes are in place to ensure that the quantity, quality and availability of these liquid resources is adequate at all times.

The Board undertakes a detailed review of its liquidity adequacy under the Internal Liquidity Adequacy Assessment Process (ILAAP) and submits this to the PRA for supervisory review. The ILAAP specifies the daily processes that the Society will use to determine the amount of liquidity required to cover its potential cash flow needs under a range of stresses including three PRA standard scenarios: 'idiosyncratic', 'market-wide' and 'combined'.

The supervisory review also informs the PRA's view of the amount of 'buffer' or highest quality liquid assets that the Society should hold to meet the three standard regulatory stress scenarios and the maximum allowable gap between maturing wholesale assets and wholesale liabilities (wholesale refinancing gap). The PRA replaced the Individual Liquidity Guidance with the Liquidity Coverage Ratio (LCR), which was a Basel III requirement to be adopted universally. Treasury maintains liquid resources at the greater of the LCR requirement or the internal assessment of liquidity adequacy.

The Board has established a Liquidity Risk Policy which lays down a rigorous framework of limits to control the Society's liquidity risk. The governance process surrounding liquidity risk management activities is as follows:

- The Board has delegated authority for the governance of Liquidity Risk Management to the Assets & Liabilities Committee (ALCo) which meets monthly;
- Operational management of liquidity risk is further delegated to the Liquidity Management Committee (LMC) which meets weekly. LMC looks at liquidity stresses over a horizon of up to three months and plans cash flows over a rolling 12 month planning period;
- Treasury is responsible for day-to-day management and maintenance of adequate liquid resources under delegated authority from ALCo; and
- The Risk Committee monitors independently the overall liquidity adequacy process, including the activities of ALCo, LMC and Treasury.

The Society is responsible for the liquidity and cash flow requirements of wholly owned subsidiaries.

Capital risk

The Society conducts an Internal Capital Adequacy Assessment Process (ICAAP) covering all risks. This is used to assess the Society's capital adequacy and determine the levels of capital required going forward to support the current and future risks in the business. This analysis is collated into an Internal Capital Adequacy Assessment (ICAA) that is approved by the Board. The ICAA incorporates expected future capital requirements from changes in business volumes, mix of assets and activities within the context of current and anticipated future risks, and multiple, stressed scenarios. The ICAA is used by the PRA to set the Society's capital requirements as Individual Capital Guidance (ICG).

Society capital requirements are reviewed on a monthly basis and the results of this monitoring are reported to the Group Capital Committee, Risk Committee and the Board.

The detailed breakdown of the Society's capital position can be found on page 18.

Operational risk

Each business function has a clearly articulated responsibility for identifying, monitoring and controlling its operational risks. The business function receives support and guidance from the Operational and Conduct Risk team, which co-ordinates regular reviews with the function managers and collates the output for review by executive management, the Operational and Conduct Risk Group and the Risk Committee.

The Operational and Conduct Risk team also provides independent input and challenge to the business functions, both through the regular review of operational risks and day-to-day business initiatives.

Retail conduct risk

Conduct risk is deemed so important that the Financial Conduct Authority (FCA) was created to increase the regulatory focus on it. This is intended to go beyond the previous focus on compliance with rules, on process and on treating customers fairly, to embrace a holistic approach of how a firm organises itself and does business in order to ensure good customer outcomes.

The management of conduct risk is a key component in the successful delivery of the Society's strategy and objectives, and protection of its members and customers.

Information risk

Understanding and managing information risk is imperative to the successful achievement of the Society's business objectives.

Effective policies, procedures and processes complemented by technological defences and detection tools, provide for successful information risk management.

To this end the Society has determined a risk management strategy based on the following principles:

- A clearly articulated and Board approved Information Risk Appetite Statement;
- A clearly articulated and Board approved information risk definition;
- An embedded and compliant Information Risk Management Framework, underpinned by robust processes and tools;
- A Board approved Cyber Resilience Strategy Plan;
- A Three Lines of Defence model with clearly articulated responsibilities for the management of information risk;
- Appropriate processes, systems and controls that support the effective management of information risks across the Society;
- Committee oversight within an appropriate governance structure; and
- An appropriate member of the senior management team with overall accountability for information risk management.

Principal risks and uncertainties

Set out in the following table are the principal external threats which have been identified by the Risk Committee, along with the Society's response and mitigants in place.

Risk category	Principal external threats	Society response and mitigants
Business risk	Adverse changes to the operating environment arising from the general uncertainty in the UK economy, following Brexit and the recently announced general election, leading to: • A further reduction in interest rates from the current historical low, or a series of rapid and large increases in interest rates to counter inflation; • Reduced activity in the housing market and possible adverse impact from both lower lending and a potential fall in house prices; • Increased competition and cost of retail funding; • Low or flat economic growth; and • Increasing regulatory costs.	Business plans continue to model the impact of a range of scenarios and stress tests to provide comfort that the Society can tolerate the consequences financially and reputationally. Income projections are reviewed regularly to identify mitigation actions.
Credit risk	Higher unemployment and/or an increase in Bank Rate (leading to increased arrears and losses).	The Society's provisioning and stress testing models assume a range of unemployment levels and varying interest rate scenarios. Should an increase occur, the Society would expand its credit management resource.
	Reduction in property prices (leading to a higher incidence of voluntary possessions).	The Society is committed to work with its borrowers to avoid possession wherever possible. In the event that possessions were to increase the Society has provided and regularly reviews its impairment provisions.
	Low or flat economic growth (leading to further tenant failures).	The Society has a well-resourced and highly experienced team dealing with commercial property mortgages and, as has been the case throughout the year, works with borrowers to lessen the impact.

Risk category	Principal external threats	Society response and mitigants
Capital risk	Rules for calculating capital (amount required and/or amount held) are changed.	Maintain regular dialogue with the regulator and ensure full understanding of the relevant rules. The European Banking Authority has been requested to confirm the treatment of profit participating deferred shares as Common Equity Tier 1 capital (as detailed in the Strategic Report on pages 8 to 22).
Liquidity risk	Intensification of competition for retail funding.	The Society continues to attract new retail savers despite intense competition.
Market risk/ Basis risk	Reduction in returns from residential tracker mortgage assets whose rate is linked to Bank Rate with no floor.	The Society does not originate any new residential tracker mortgages and is managing down its Base Rate Tracker book.
	Falling HPI, leading to a reduction in the book value of West Bromwich Homes Limited properties.	No new homes are being added to the portfolio and active steps are being taken to reduce the Society's exposure.
Operational risk	Insurance arrangements do not sufficiently cover an event (requiring the Society to pick up the cost).	The annual review of insurance arrangements is based on advice from brokers and an annual benchmarking exercise.
	A significant business continuity event.	Detailed business plans are in place, which are regularly tested.
Information risk	One or more of the Society's IT systems are attacked for the purposes of financial gain, theft of data or to cause the Society disruption or negative exposure and threaten the security of members' information, and the availability of the services offered to them. Cyber attacks remain a significant risk for financial institutions.	The Society recognises the need to maintain and develop its defences and responses in this area in order to protect the Society and maintain the trust of customers and the confidence of regulators. External specialist advice has been received and actions implemented on system design. During 2016/17, the Society invested significantly in cyber security infrastructure and training and will continue to do so in 2017/18, in line with the Cyber Resilience Strategy and Information Risk Management Framework. This will require the Society to remain vigilant to the latest cyber attack trends and protection defences.
Pension liability risk	Increased longevity and/or poor investment returns (requiring the Society to contribute more to the scheme).	The defined benefit scheme is closed to new members and existing members are no longer accruing service benefits. The Trustees take extensive advice (actuarial, investment etc.) to minimise the impact of the risks identified.
Retail conduct risk	Actions of third party suppliers leading to adverse customer outcomes.	A robust supplier framework is in place to oversee the activities of key suppliers.

The Society has a Recovery Plan in place that captures inter alia management actions for a range of adverse scenarios that may impact any of the above risks either individually or collectively.

Richard Sommers
Chairman of Risk Committee
30 May 2017

Board of Directors

Back row left to right: **Jonathan Westhoff, Claire Hafner** and **Ashraf Piranie.**
Front row left to right: **Julie Hopes** and **Martin Ritchley.**

Claire Hafner MA, ACA
Age 57 / Non-Executive Director Appointed September 2011
Claire is currently Chief Financial Officer of Fintrax Group Holdings Ltd. She was previously Chief Financial Officer for VocaLink, a specialist provider of transaction services to banks, their corporate customers and to the public sector and Finance Director for law firm Eversheds, heading a team of finance professionals across the UK and overseas. Claire is a member of the Audit, Risk and Remuneration committees.

Julie Hopes MBA, ACIB
Age 49 / Non-Executive Director Appointed April 2016
Julie has many years of experience in retail financial services, with a particular focus on general insurance. An Associate of the Chartered Institute of Bankers, she has Non-Executive Director roles with Co-operative Insurance and the Police Mutual Assurance Society. Julie is a member of the Risk Committee.

Mark Nicholls MA (Cantab), MBA
Age 68 / Chairman Appointed January 2010
Mark has considerable knowledge of financial services having been a Director of SG Warburg Group Plc and Managing Director of the private equity group of the Royal Bank of Scotland. Mark has held Non-Executive Directorships at Portman and Nationwide building societies and is currently Chairman of Rathbone Brothers Plc. Mark also has a longstanding commitment to the charitable and public sector. Mark chairs the Nominations Committee and is a member of the Remuneration Committee.

Ashraf Piranie FCCA, MBA
Age 53 / Group Finance & Operations Director Appointed March 2017
Ashraf has worked in financial services for most of his working life, including the positions of Finance Director and Joint Managing Director at the Islamic Bank of Britain and Director of Finance at Alliance & Leicester Plc. Prior to joining the West Brom, he was Deputy Chief Executive & Finance Director at Nottingham Building Society. Ashraf is also Deputy Chair of the PRA Practitioner Panel. Ashraf chairs the Society's Assets & Liabilities Committee.

Mark Preston BA (Hons), ACIB
Age 57 / Non-Executive Director Appointed May 2011
Mark has been involved in financial markets for nearly 30 years, most recently as Chief Executive at Exotix Partners. He was previously Chief Executive Officer for the Products and Markets Division of Lloyds TSB and Co-Head of the Bank's Corporate Markets. Mark is a member of the Risk and Remuneration committees.

Back row left to right: **Mark Preston** and **Richard Sommers.**
Front row left to right: **James Turner, Colin Walklin** and **Mark Nicholls.**

Martin Ritchley FCA, FCIB, Hon DBA (Coventry)
Age 70 / Deputy Chairman and Senior Independent Director Appointed September 2009
Martin is a former Chief Executive of Coventry Building Society and former Chairman of the Building Societies Association. He chairs the Remuneration Committee and is a member of the Audit, Nominations and Risk committees.

Richard Sommers MA (Oxon), ACIB
Age 60 / Non-Executive Director Appointed October 2009
Richard is highly experienced in retail and commercial banking and held senior positions with the Barclays Group, including Chief Financial Officer for Barclaycard and Risk Director of Retail Financial Services. He has also been Treasurer and Fellow of Lady Margaret Hall, a college in the University of Oxford, before retiring in 2016, and is now an Emeritus Fellow. Richard chairs the Risk Committee and is a member of the Audit and Nominations committees.

James Turner FCA, FCSI, BA (Hons)
Age 47 / Non-Executive Director Appointed April 2017
James is the Director of Group Finance at Prudential plc. Prior to Prudential, James was the Deputy Head of Compliance for Barclays. He also held a number of senior internal audit roles across the Barclays Group leading teams that focussed on global retail and commercial banking activities. James is a member of the Audit and Risk committees.

Colin Walklin BSc, FCA
Age 63 / Non-Executive Director Appointed July 2011
Colin is Group Chief Operating Officer of Standard Life plc with responsibility for operations, technology and change management throughout the Group. A qualified Chartered Accountant, Colin chairs the Audit Committee and is a member of the Risk Committee.

Jonathan Westhoff BA (Hons) Financial Services, FCMA, CGMA, ACIB
Age 52 / Chief Executive Appointed May 2009
Formerly the Society's Group Finance Director and Deputy Chief Executive, Jonathan was appointed as Chief Executive in May 2011. After 17 years with Barclays Bank, he moved into the mutual sector in 2000, serving as Finance Director at Portman and Newcastle building societies. Jonathan is currently Chairman of the Building Societies Association and a Councillor on the CBI West Midlands Council. He chairs the Executive Committee and is a member of the Society's Assets & Liabilities Committee.

Directors' Report

The Directors are pleased to present their Annual Report, together with the audited Accounts, for the financial year ended 31 March 2017.

Business objectives

The main purpose of the Society and its subsidiaries (the Group) is to work together to meet the prime financial needs of our members. This entails provision of a range of personal financial services, offering competitive pricing and excellent service.

Business review

The Group's business and future plans are referred to in the Chairman's Statement on page 2, the Chief Executive's Review on pages 4 to 7 and the Strategic Report on pages 8 to 22.

Key performance indicators

The Board measures performance against its strategic aims by reference to a number of key performance indicators which are described in the Strategic Report on pages 8 to 22.

Profit and capital

The Group's loss before tax (on continuing operations) amounted to £19.8m (2015/16: profit of £13.5m). The total loss after tax transferred to reserves was £25.8m (2015/16: profit of £9.4m).

The total Group reserves at 31 March 2017 were £215.5m (2015/16: £243.3m) after taking into account a revaluation reserve of £3.5m (2015/16: £3.4m), a cash flow hedging reserve deficit of £0.7m (2015/16: £0.3m) and an available for sale reserve of £1.7m (2015/16: £0.9m).

Gross capital at 31 March 2017 was £463.5m (2015/16: £497.7m) including £173.0m of profit participating deferred shares (2015/16: £179.5m) and £75.0m (2015/16: £74.9m) of subscribed capital.

The main Group ratios were as follows: gross capital ratio; 9.25% (2015/16: 10.37%), free capital ratio; 6.21% (2015/16: 7.29%) and liquidity ratio; 17.04% (2015/16: 17.28%). For further details see page 111.

Detailed Pillar 3 capital disclosures for the current year will be available on the Society's website.

Country-by-country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 place certain reporting obligations on financial institutions that are within the scope of the Capital Requirements Directive (CRD IV).

The principal activities of the Society are set out under the business objectives earlier in this report and, for each of the Society's subsidiaries, in note 15 to the Accounts. All of the activities of the Group are carried out in the United Kingdom and therefore 100% of the total income, profit before tax and tax shown in the Income Statement as well as employee figures shown in note 7 are related to the United Kingdom. The Society and its subsidiaries have not received any public subsidies (2015/16: nil).

Risk management

As the Society operates in a very competitive environment, the management of risk and development of a suitable strategy are critical activities in achieving business success.

The Board and the Board Committees ensure that risk management and strategic direction are considered regularly and that appropriate actions are implemented. These considerations are detailed in the Society's Internal Capital Adequacy Assessment Process (ICAAP) document.

The principal risks inherent to our business and details of how these risks are managed are set out in the Risk Management Report on pages 23 to 27.

In addition to these principal risks there are, as a result of the economic environment for banks and building societies, ongoing actions under the PRA's supervisory review process, which include extensive stress testing exercises. The Directors are aware, in arriving at their judgements, that the Society will be subject, in the same way as others within the sector, to these ongoing tests of capital and recognise the uncertainty inherent in the process as factors within each test change.

Financial risk management objectives and policies

The Board's objective is to minimise the impact of financial risk upon the Society's performance. Financial risks faced by the Society include interest rate, credit and liquidity risks. The Board manages these risks through a risk management framework, Board policies and its Treasury and Credit Risk functions. Governance and oversight is provided through the Risk and Assets & Liabilities Committees. Details of the Society's financial instruments, hedging activity and risk mitigation can be found in note 12 and notes 31 to 34 to the Accounts.

Mortgage arrears

At 31 March 2017 there were 39 (2015/16: 73) residential and commercial mortgage accounts where payments were 12 months or more in arrears based on current monthly repayments. The total amount outstanding on these accounts was £87.7m (2015/16: £74.1m), representing 1.85% (2015/16: 1.57%) of mortgage balances, and the amount of arrears was £13.5m (2015/16: £13.9m). Appropriate provisions were made for potential losses on mortgages in accordance with the provisioning policy set out in note 1 to the Accounts.

Directors

The following served as Directors of the Society during the year:

Mark Gibbard*
Claire Hafner
Julie Hopes
Mark Nicholls (Chairman)
Ashraf Piranie*
Mark Preston
Martin Ritchley
Richard Sommers
Colin Walklin
Jonathan Westhoff*

* Executive Directors.

All Directors are members of the Society. None of the Directors have, at any time in the year or as at the year end, any beneficial interest in shares or debentures of any associated body of the Society.

Supplier payment policy

The Society's policy is to agree the terms of payment before trading with the supplier and to pay in accordance with its contractual and other legal obligations. At 31 March 2017, the creditor days figure was 26 days (2015/16: 21 days). This conforms with the aim of paying creditors promptly.

Charitable donations

During the year the Society donated £17,603 (2015/16: £18,600) to charitable organisations. The Society also raised significant sums through its community programme, affinity accounts and voluntary staff initiatives. These are outlined on page 21 of the Strategic Report.

No donations were made for political purposes. While encouraging any employees who wish to take part in community affairs, the Group does not support any employees in the pursuit of political activity.

Employees

The Society is an equal opportunities employer and gives proper consideration to all applications for employment with regard to vacancies that arise and to the applicant's own aptitude and abilities, regardless of race, creed, gender, sexual orientation, marital status, age, physical or mental disability. If current staff members become disabled, every effort is made to enable them to maintain their present position or to receive relevant retraining.

The Society was one of the first signatories to the Women in Finance initiative, which is a government sponsored initiative to increase the numbers of female staff in financial services. The Society has committed to producing a diversity strategy during 2017 to increase its representation of people from all backgrounds.

The Society has systems that provide information to employees, permitting them to participate in the operation and development of the business. The Society consults with the West Bromwich Building Society Staff Union and assesses the results of staff satisfaction surveys to ensure that staff conditions and workload are maintained at an acceptable level. Additionally, details of meetings, team briefings, circulars and information updates are placed on the Society's intranet to ensure that employees are aware of the Society's objectives and performance and conscious of the wider financial and commercial environment in which the Society operates.

Health and safety

The Society sets high standards to maintain the health and safety of all staff, customers and those affected by any of its operations.

The Society is committed to ensuring that all employees receive adequate training in health and safety to make them aware of their individual responsibilities to enable them to carry out their work without injury or damage to the health of themselves or others affected by their work. All employees, on commencing employment with any business area, receive induction training which is reinforced through annual refresher training. Additional training is delivered when a need has been identified, such as Manager Training, Stress Awareness, Manual Handling, Fire Warden, First Aid etc.

The Society recognises the need to consult with its employees on health and safety issues. Accredited safety representatives are afforded every opportunity to effect this consultation and to receive training. A Health and Safety Committee is in place with representatives from across the business which meets quarterly to review health and safety.

Health and safety issues are brought to the attention of all employees through business specific communication channels. Employees are similarly encouraged to raise issues through their line management.

During the reporting year no enforcement notices were issued against the organisation by any of the enforcing authorities and no proceedings were instigated against the Society for breaches of health and safety regulations within the reporting period.

Directors' responsibilities in respect of the Annual Report, the Annual Business Statement, the Directors' Report and the Annual Accounts

The Directors are responsible for preparing the Annual Report, Annual Business Statement, 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 Group and Society Annual Accounts for each financial year. Under that law they are required to prepare the Group Annual Accounts in accordance with International Financial Reporting Standards (IFRS) as adopted by the EU and applicable law and have elected to prepare the Society Annual Accounts on the same basis.

The Group and Society Annual Accounts are required by law and IFRS, as adopted by the EU, to present fairly the financial position and the performance of the Group and the Society; the Building Societies Act 1986 provides in relation to such Annual Accounts that references in the relevant part of that Act to Annual Accounts giving a true and fair view are references to their achieving a fair presentation.

In preparing each of the Group and Society 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 they have been prepared in accordance with IFRS as adopted by the EU; and
- prepare the Annual Accounts on the going concern basis unless it is inappropriate to presume that the Group and 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 Group and Society.

A copy of the Annual Accounts is placed on the Society's website.

Directors' statement pursuant to the Disclosure and Transparency Rules

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware:

- the financial statements, prepared in accordance with IFRS, as adopted by the EU, give a true and fair view of the assets, liabilities, financial position and result of the Group; and
- the management reports in pages 8 to 27 include a fair review of the development and performance of the business and the position of the Group and Society, together with a description of the principal risks and uncertainties that they face.

Directors' responsibilities for accounting records and internal control

The Directors are responsible for ensuring that the Group:

- 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; and
- takes reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with 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 Group 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 United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Directors' responsibilities in respect of going concern

In preparing the financial statements the Directors must satisfy themselves that it is reasonable for them to conclude it is appropriate to adopt the going concern basis. The Group meets its day-to-day liquidity requirements through managing both its retail and wholesale funding sources and is required to maintain a sufficient buffer over regulatory capital requirements in order to continue to be authorised to carry on its business.

The Group's business activities, together with the factors likely to affect its future development, performance and position are set out in the Chief Executive's Review on pages 4 to 7 and the Strategic Report on pages 8 to 22. The financial position of the Group, its capital structure and risk management and control processes for managing exposure to credit, market, liquidity and operational risk are described in the Strategic Report on pages 8 to 22 and the Risk Management Report on pages 23 to 27.

In addition, notes 31 to 34 to the Accounts include further information on the Group's objectives, policies and processes for managing its exposure to liquidity, credit and interest rate risk, details of its financial instruments and hedging activities.

The Group's forecasts and projections take account of possible changes in trading performance and funding retention and include stress testing and scenario analysis, with due regard given to the third party challenge over the eligibility of the Society's profit participating deferred shares to be treated as Common Equity Tier 1 capital. The forecasts show that the Group will be able to operate at adequate levels of both liquidity and capital for the foreseeable future. Furthermore, the Group's capital is in excess of the PRA requirement under each of the scenarios considered.

After making enquiries, the Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future and that, therefore, it is appropriate to adopt the going concern basis in preparing the Annual Accounts.

Auditor

The auditor, KPMG LLP, has expressed their willingness to continue in office. In accordance with Section 77 of the Building Societies Act 1986, a resolution for their re-appointment will be proposed at the Annual General Meeting.

The Directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Society's auditor is 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 auditor is aware of that information.

By order of the Board

Mark Nicholls
Chairman
30 May 2017

Directors' Report on Corporate Governance

The Board is committed to high standards of corporate governance and believes they are central to the Society's culture and values.

The widely accepted articulation of good practice is the UK Corporate Governance Code (the Code).

The Society is not required to and does not comply with the Code, as it applies to publicly listed companies, but where it is considered relevant, the Society does have regard to its principles. This Report details the Society's approach to corporate governance and, where different to relevant Code principles, explains why that is the case.

The Code's Main Principles	What the Society does to meet the Principles
A1 The Role of the Board Every company should be headed by an effective board which is collectively responsible for the long-term success of the company.	The principal functions of the Society's Board include: • Providing entrepreneurial leadership; • Setting the Society's strategic aims and risk appetite; • Implementing and maintaining a framework of prudent and effective controls, which enables risk to be assessed and managed; • Ensuring the necessary financial and human resources are in place for the Society to meet its objectives; and • Reviewing management performance. The Board meets as often as is necessary to fulfil its responsibilities. During the last financial year the Board met on 12 occasions. Details of Director attendance at Board and Committee meetings can be found in the table at the end of this Report. The minutes of Board and Committee meetings record all material discussion and challenge and are circulated to all Directors. The Chair of each Committee reports to the subsequent Board meeting the key matters discussed. A schedule of matters reserved to the Board is maintained and kept under regular review. The Board is supported by a number of Committees each with Board approved terms of reference. Details of the membership of those Committees and their key activities are reported elsewhere in this Report and Accounts. The Society has arranged appropriate insurance cover in respect of legal action against its Directors.
A2 Division of Responsibilities There should be a clear division of responsibilities at the head of the company between the running of the board and the executive responsibility for the running of the company's business. No one individual should have unfettered powers of decision.	The positions of Chairman and Chief Executive are held by different people. The role of the Chairman includes establishing and developing an effective Board to provide support and constructive challenge to the management team. Further details of the Chairman's main responsibilities are set out in the commentary relating to Code Principle A3. The Chief Executive has overall responsibility for managing the Society and implementing Board agreed strategy.
A3 Chairman The chairman is responsible for leadership of the board and ensuring its effectiveness on all aspects of its role.	The main responsibilities of the Chairman are: • Establish and develop an effective Board, including succession planning, recruitment and appraisal of Non-Executive Directors (NEDs); • Lead the Board as a team; • Ensure that the Board has agreed clear values and guiding principles; • Plan and manage the Board's business, including ensuring that appropriate committees are established with the right objectives and membership and that the Board has the right agenda and information; • Ensure that the Board has established key priorities; • Maintain and develop a productive and open relationship with the Chief Executive, agree the Chief Executive's objectives and carry out regular appraisals. The Chairman is responsible for leading the appointment process for the Chief Executive; • Ensure there are appropriate arrangements for the evaluation and remuneration of senior executives; • Act as an accountability focus for the Society, including chairing the Annual General Meeting; • Represent the Society with Regulators and ensure that there is an open and trustworthy relationship; and • Ensure that the Board and its Committees periodically evaluate their own performance. The Board has satisfied itself that both at the time of his appointment, and currently, the Chairman is independent in character and judgement and meets the independence criteria set out in the Code.
A4 Non-Executive Directors As part of their role as members of a unitary board, non-executive directors should constructively challenge and help develop proposals on strategy.	NEDs are involved in all key decisions and receive detailed management information and reports to ensure they have a firm grasp of the Society's business and external operating environment. NEDs are responsible for all appointment, termination and remuneration decisions relating to the Society's Executive Directors. Martin Ritchley has been appointed as the Board's Senior Independent Director (he is also Deputy Chairman). As Senior Independent Director he leads the annual review of the Chairman's performance. The NEDs meet formally and informally without Executive Directors present.

The Code's Main Principles	What the Society does to meet the Principles
B1 The Composition of the Board The board and its committees should have the appropriate balance of skills, experience, independence and knowledge of the company to enable them to discharge their respective duties and responsibilities effectively.	Board and Committee composition is kept under regular review by the Chairman and the Nominations Committee to ensure that it is of appropriate size, mix of Executive and Non-Executive Directors and has the right skills and experience to oversee the Society's business activities. The Board believes that all NEDs should meet the Code's independence criteria on appointment and throughout their term of office and has determined that each of the current Directors is independent in character and judgement and that there are no potential conflicts of interest which would affect their judgement.
B2 Appointments to the Board There should be a formal, rigorous and transparent procedure for the appointment of new directors to the board.	During the course of the last financial year Mrs Julie Hopes joined the Board in the role of NED on 1 April 2016. In addition, Mr Ashraf Piranie joined the Society on 13 March 2017 as Group Finance & Operations Director. Mr Piranie succeeds Mr Mark Gibbard who retired from the Board on 31 March 2017. During the latter part of the financial year the search began for an additional NED to join the Board. The process involved the support of a specialist recruitment firm in the search and interview process. Initially, all individuals identified by the recruitment firm were reviewed by members of the Board to identify a shortlist of potential candidates to interview. These candidates were then interviewed by the recruitment firm before being interviewed by members of the Board. The potential successful candidate then met with the remaining Board members and Group Secretary. Finally, the Nominations Committee recommended to the Board that the potential candidate be offered the role of NED. The process concluded with the appointment of Mr James Turner who joined the Board on 1 April 2017. The terms of reference of the Nominations Committee, which is made up of NEDs only, is available on request from the Group Secretary.
B3 Commitment All directors should be able to allocate sufficient time to the company to discharge their responsibilities effectively.	The standard letter of appointment for NEDs sets out the expected time commitment and explains what is required if there is any material change to their commitments.
B4 Development All directors should receive induction on joining the board and should regularly update and refresh their skills and knowledge.	The Society has a range of induction activities and material for NED appointments which is tailored to their individual experience. These include site visits, meetings with senior management and reports/information concerning the Group's operations. Internally organised events on topics of particular relevance to the Society are used to aid development. NEDs are also encouraged to attend appropriate externally organised events. A development log records relevant development activities undertaken by individual Directors.
B5 Information and Support The board should be supplied in a timely manner with information in a form and of a quality appropriate to enable it to discharge its duties.	Board papers, including a management information pack are issued to Directors prior to Board meetings. Board agendas are agreed in advance of each meeting and focus on strategic matters, as well as ensuring that Directors are kept informed of key business activities and regulatory developments. Minutes of Board Committee meetings held since the last Board meeting are included in the papers. Where appropriate, papers are presented by the relevant member of the management team. The Board and its Committees are served by the Group Secretary who advises on governance matters and procedures. Directors have access to independent professional advice should that be required.
B6 Evaluation The board should undertake a formal and rigorous annual evaluation of its own performance and that of its committees and individual directors.	The most recent formal evaluation of Board effectiveness was initiated in the latter part of the 2016/17 financial year. As a result of the changes to the Board composition during the year, this evaluation will be conducted over the financial years 2016/17 and 2017/18. This evaluation will be conducted by an external firm with expertise in this area. The process will involve interviewing all Board members, as well as key individuals who regularly interact with the Board. In addition, meetings of both the Board and Risk Committee will be observed. The process will culminate in a report to the Board, to be presented at the January 2018 meeting. The annual evaluation of the Chairman was led by the Deputy Chairman and took the form of a meeting to review the effectiveness of the Chairman and Board and Committee provisions. The conclusions were shared with the Chairman.
B7 Re-election All directors should be submitted for re-election at regular intervals, subject to continued satisfactory performance.	All new Directors are required by the Society's Rules to stand for election at the first Annual General Meeting following their appointment to the Board. The Code's Main Principle relating to re-election of Directors requires that they be submitted for re-election at regular intervals. One of the Supporting Provisions is that all Directors of FTSE 350 companies should be subject to annual election. Although the Society is not a FTSE 350 company, the Board would normally adopt Code Provisions which apply to such firms. Having carefully reviewed the Provision, the Board has concluded that, although very unlikely, there could be circumstances where requiring all Directors to stand for election could have an adverse outcome for the stability of the Society and that this would not be in the best interests of members. The Society's Rules require that those Directors who are due for election or who have not been re-elected in the last three years must stand for election/re-election. James Turner, appointed on 1 April 2017, will stand for election in July 2017. In addition, Ashraf Piranie, appointed on 13 March 2017, will also stand for election. All of the other Directors were re-elected in 2015 or 2016 and are therefore not required by the Rules to stand for re-election in 2017. However, recognising the Code Provision, the Board believes that it would be appropriate to bring forward the re-election (as permitted by the Rules) of four Directors so that half of the Board is standing for re-election in 2017. The Rules also state that any Director reaching the age of 70 should stand for re-election. Martin Ritchley reaches the age of 71 on 1 July 2017 and therefore has been put forward for re-election this year. The Board has agreed to keep the arrangements under review and will explain any variation to the Code in future Corporate Governance Reports.
C1 Financial and Business Reporting The board should present a fair, balanced and understandable assessment of the company's position and prospects.	The Directors' Report on pages 30 to 32 includes statements detailing the Directors' responsibilities. The Chief Executive's Review on pages 4 to 7, the Strategic Report on pages 8 to 22 and the Risk Management Report on pages 23 to 27, give an extensive report on the Society's performance, financial position and the key risks that will impact performance and risk management going forward.

The Code's Main Principles	What the Society does to meet the Principles
C2 Risk Management and Internal Control The board is responsible for determining the nature and extent of the significant risks it is willing to take in achieving its strategic objectives. The board should maintain sound risk management and internal control systems.	The Society's Board is responsible for the development of strategies relating to risk management and internal control. Operational responsibility rests with the Executive Directors and senior managers. The risk management systems and internal controls are designed to allow the Society to achieve its objectives in a controlled manner and remain within defined risk appetite statements. These systems and controls are designed to manage rather than eliminate risk. The Board reviews the effectiveness of the risk management systems and internal controls in a number of ways, including: • Board review and approval of Risk Appetite Statements at least annually, with monthly reporting relating to those statements; • A formal committee structure, including an Audit Committee (see below for more detail) and a Risk Committee. The minutes of the meetings of these Committees are reviewed by the full Board, the relevant Committee Chairman highlighting any key issues; • Regular reports and presentations to the Board by the Executive Directors; and • Monthly Board report on key business performance. The Society's Internal Audit function, with a dual reporting line to the Chief Executive and Chair of Audit Committee, provides independent assurance regarding the adequacy and effectiveness of internal controls across all Group activities.
C3 Audit Committee and Auditors The board should establish formal and transparent arrangements for considering how they should apply the corporate reporting and risk management and internal control principles and for maintaining an appropriate relationship with the company's auditor.	The Board has an Audit Committee comprising four NEDs, all of whom are considered independent according to the criteria contained in the Code. The Board is satisfied that at least one member of the Committee has recent and relevant financial experience. The Chairman of the Audit Committee receives additional fees in recognition of his added responsibilities. The terms of reference of the Committee are available from the Group Secretary on request. The Society has a policy on the engagement of external auditors to supply non-audit services, which is operated across the Group and in tandem with the external auditor's own internal policy on providing non-audit services. The Society has a well established 'Open Door' Policy to enable staff to raise concerns in confidence about possible improprieties in matters of financial reporting or other issues. This policy has taken account of the Public Interest Disclosure Act 1998. During the year, the Committee received a report summarising all of the reports made under this Policy. There have been four meetings of the Committee during the financial year 2016/17. Executive Directors and other members of senior management (by invitation only) attended the meetings. Those employees who regularly attend include the Chief Executive, Group Finance & Operations Director, Group Secretary, Chief Financial Risk Officer and Divisional Director Internal Audit. The Board receives regular reports on Committee meetings and also receives copies of the minutes of these meetings. During the last financial year, the Audit Committee: • Validated the integrity of the Group's financial statements (including formal announcements relating to such statements); • Reviewed and approved significant financial reporting issues and accounting policies/issues; • Reviewed the Group's internal controls; • Monitored and reviewed the effectiveness of the Group's Internal Audit function; • Recommended the appointment of the external auditor (following a review of the external auditor's independence and objectivity and the effectiveness of the audit process), the remuneration and terms of engagement; • Confirmed that the Internal Audit function was appropriately resourced; and • Met privately with the Divisional Director Internal Audit and the external auditor.
D1 Level and Components of Remuneration Levels of remuneration should be sufficient to attract, retain and motivate directors of the quality required to run the company successfully, but a company should avoid paying more than is necessary for this purpose. A significant proportion of executive directors' remuneration should be structured so as to link rewards to corporate and individual performance. **D2 Procedure** There should be formal and transparent procedure for developing policy on executive remuneration and for fixing the remuneration packages of individual directors. No director should be involved in deciding his or her own remuneration.	The Board has established a Remuneration Committee, comprising four NEDs, which considers and makes recommendations to the Board on key remuneration decisions relating to Society staff who have been identified in the FCA's Remuneration Code as Code Staff. The Directors' Remuneration Report on pages 40 to 46 explains how the Society, through the Remuneration Committee and Board, approaches the remuneration of Directors and other executives. The Society is subject to the FCA's Remuneration Code, requiring the Society to have a remuneration policy which promotes effective risk management, supports business strategy, objectives and values, and is in the long-term interests of the Society. During the last financial year, the Remuneration Committee: • Reviewed the Society's Remuneration Policy; • Recommended to the Board the Performance-Related Pay Scheme and awards under that Scheme; • Reviewed employee benefits arrangements; • Made recommendations to the Board in respect of the annual salary review; • Reviewed the employee benefits package; and • Reviewed the terms of appointment and benefits of Code Staff.

The Code's Main Principles	What the Society does to meet the Principles
E1 Dialogue with Stakeholders There should be a dialogue with shareholders based on the mutual understanding of objectives. The board as a whole has responsibility of ensuring that a satisfactory dialogue with shareholders takes place.	As a mutual, the Society is owned by its members; the Society seeks feedback from members in a number of ways, including: • Regular Members' ViewPoint events held around the branch network; • Assessing enquiries from the Society's contact centre and website; • Analysing the quantity and nature of customer complaints; • Customer research on specific topics; • Customer satisfaction surveys and Mystery Shopper programme; and • Customer Panel to canvass views on products and services and give feedback on how we can improve the way we operate.
E2 Constructive Use of the AGM The board should use the AGM to communicate with investors and to encourage their participation.	All members who are eligible to vote are sent a Summary Financial Statement and details of the Annual General Meeting (AGM) at least 21 days before the date of the meeting. Proxy forms are also included in the AGM mailing to allow those members who do not attend the meeting to cast their vote. Members are also able to submit their proxy form electronically. The Society uses independent scrutineers to count proxy votes received through the post and via the internet. All Board members are expected to be present at the AGM each year (except in the case of unavoidable absence). The Chairmen of the Audit, Remuneration, Risk and Nominations Committees are available to answer questions at the AGM.

Meetings of the Nominations Committee

The Nominations Committee which is chaired by the Society's Chairman, met on five occasions in the last financial year. The key matters considered by the Committee were:

- Membership of Board committees;
- Board performance evaluation arrangements;
- NEDs reaching the end of their three year term of office;
- NED development; and
- Board Succession Planning.

The terms of reference of the Committee, which is made up of NEDs only, is available on request from the Group Secretary.

The attendance of individual Directors during the year, with the number of meetings each was eligible to attend shown in brackets, is set out below.

Attendance records – Board and Board Committee meetings

	Board	Nominations	Audit	Risk	Remuneration
Mark Nicholls	12 (12)	5 (5)			6 (6)
Mark Gibbard	12 (12)				
Claire Hafner	12 (12)		4 (4)	8 (9)	6 (6)
Julie Hopes	11 (12)			8 (9)	
Ashraf Piranie	1 (1)				
Mark Preston	10 (12)			8 (9)	6 (6)
Martin Ritchley	12 (12)	5 (5)	4 (4)	9 (9)	6 (6)
Richard Sommers	12 (12)	5 (5)	4 (4)	9 (9)	
Colin Walklin	12 (12)		4 (4)	6 (9)	
Jonathan Westhoff	12 (12)				

Mark Nicholls
Chairman
30 May 2017

Audit Committee Report

Membership and attendees

The Audit Committee is appointed by the Board and, at 31 March 2017, comprised four Non-Executive Directors:

- Colin Walklin (Chairman);
- Claire Hafner;
- Martin Ritchley; and
- Richard Sommers.

The Chairman, Chief Executive, Group Finance & Operations Director, Chief Financial Risk Officer, Group Secretary, Divisional Director Treasury & Finance, the external auditor and Divisional Director Internal Audit also attend by invitation.

The Board is satisfied that the Committee has members with recent and appropriate financial experience.

The Committee met four times during the year, with attendance as detailed on page 36. In addition, the Committee met privately with the external auditor and the Divisional Director Internal Audit.

Roles and responsibilities

The roles and responsibilities of the Committee are in line with the provisions of the Financial Reporting Council (FRC) Guidance on Audit Committees (the 'Smith Guidance') which was updated in September 2012 and applied for financial years beginning on or after 1 October 2012.

The main function of the Committee is to assist the Board in fulfilling its oversight responsibilities in relation to:

- the provision of assurance to the Board regarding the integrity of the financial statements of the Society, including its annual and any interim reports, reviewing significant financial reporting issues and judgements which they contain. The Committee also review summary financial statements and significant financial returns to regulators;
- assessing the adequacy and effectiveness of the Society's internal controls and risk management systems (including conduct risk);
- reviewing and approving the statements to be included in the Annual Report concerning internal controls and risk management;
- reviewing the Society's arrangements for its employees to raise concerns, in confidence, about possible wrongdoing in financial reporting or other matters. The Committee shall ensure that these arrangements follow proportionate and independent investigation of such matters and appropriate follow up action;
- monitoring and reviewing the effectiveness of the Society's Internal Audit function in the context of the Society's overall risk management system;
- approving the appointment and removal of the Divisional Director Internal Audit, and making recommendations regarding performance objectives and remuneration to the Society's Remuneration Committee as required;
- considering and approving the remit of the Internal Audit function and ensuring it has adequate resources and appropriate access to information to enable it to perform its function effectively and in accordance with the relevant professional standards. The Committee shall also ensure the function has adequate standing and is free from management or other restrictions;
- reviewing and assessing the Internal Audit plan;
- considering and making recommendations to the Board, to be put to members for approval at the Annual General Meeting (AGM), in relation to the appointment, reappointment and removal of the Society's external auditor. The Committee shall oversee the selection process for new auditors and if an auditor resigns, the Committee shall investigate the issues leading to this and decide whether any action is required;
- monitoring the effectiveness of the Society's external auditor, including (but not limited to):
  - approval of their remuneration, whether fees for audit or non-audit services, and ensuring that the level of fees is appropriate to enable an adequate audit to be conducted;
  - approval of their terms of engagement, including any engagement letter issued at the start of each audit and the scope of the audit;
  - assessing annually their independence and objectivity taking into account relevant UK professional and regulatory requirements and the relationship with the auditor as a whole, including the provision of any non-audit services; and
  - reviewing and approving in accordance with policy, any proposed employment of employees or former employees of the Society's auditor.

The minutes of the Audit Committee are distributed to the Board, and the Committee Chairman provides a verbal report to the Board meeting immediately following Committee meetings.

A copy of the Audit Committee terms of reference can be obtained from the Group Secretary, on request.

Areas of focus for the Committee in the year

The Committee has an annual schedule, developed from its terms of reference, with standing items that it considers at each meeting in addition to any specific matters upon which the Committee has decided to focus. The work of the Audit Committee falls under three main areas as follows:

a) Financial reporting issues and judgements

The Committee considers the financial information published in the Society's annual and half year financial statements and considers the accounting policies adopted by the Society, presentation and disclosure of the financial information and, in particular, the key judgements made by management in preparing the financial statements. The Committee pays particular attention to matters it considers to be important by virtue of their impact on the Society's results, and particularly those which involve a high level of complexity, judgement or estimation by management.

The Committee also take note of the work of the external auditor, KPMG LLP, to help ensure that suitable accounting policies have been implemented and appropriate judgements have been made by management.

Since the previous year end, there have been no changes in the Group's accounting policies. The key matters that the Committee considered in reviewing the 2016/17 financial statements were:

- **Loan impairment provisions**
  Review and confirmation of the approach adopted in calculating loan loss provisions, including an assessment of the appropriateness of the assumptions which may, in particular for commercial loans, include the length of period the properties are held in order to manage the exposure. The Committee was satisfied with the overall approach and quantum of impairment provisions along with the applicable disclosures included in the Annual Accounts.

- **Other provisions**
  Provisions at the year end date primarily relate to the Society's participation in the Financial Services Compensation Scheme and estimated future costs of payment protection insurance (PPI) redress. Management have conducted a full review to ensure there are no new present obligations, arising from past events, which require the recognition of a provision or disclosure of a contingent liability.

  The Committee has considered management's assessment and agreed the reasonableness of the overall level of provisions disclosed in the financial statements.

- **Income recognition**
  The Group recognises mortgage income using the effective interest method, which includes an estimation of the expected behavioural life of the loan. The Committee has confirmed the appropriateness of the income recognition calculations and assumptions.

- **Investment property valuations**
  The Group continues to hold a significant investment property portfolio where it has adopted the fair value model of measurement. The Committee has reviewed and confirmed the appropriateness of the process and assumptions applied in calculating the fair value of the property portfolio at the end of the financial year. It is satisfied that the valuation reflects all assumptions that market participants would use when pricing the investment properties under the current market.

- **Deferred taxation**
  The Group holds a deferred tax asset on its balance sheet, predominantly arising from losses incurred over the period 2008/9 to 2012/13. During the year, the Court of Appeal overturned an earlier decision of the High Court in respect of the Group's ability to vary the interest rate on certain loans. This affects the Group tax charge by extending the timeframe over which the deferred tax asset is expected to be recovered. Consequently no tax credit is recognised against the loss for the year and a charge of £6.0m has been recorded to write down the value of the brought forward deferred tax asset to a level which the Committee deems recoverable in the next five years, based upon the detailed forecasts included within the Group's Medium Term Plan.

- **Capital disclosures**
  During the year, a third party challenged the eligibility of the Society's profit participating deferred shares (PPDS) to be treated as Common Equity Tier 1 (CET1) capital. The Committee's view, pending clarification from the European Banking Authority, is that the PPDS are qualifying CET1 capital. The Committee is therefore satisfied with the disclosure of the PPDS as CET1 in the Annual Report and Accounts.

- **Going concern**
  The Committee has reviewed the adoption of the going concern assumption for the interim and year end accounts, adopting the same, thorough approach for both reporting periods. This involved a rigorous consideration of the sufficiency of current and projected capital and liquidity positions together with the principal risks which could impact these positions, including the capital treatment of PPDS described above. The Committee also reviewed the viability of the business model in terms of recurring level of profitability, support from the regulator and ability to continue to trade. Based on this review, the Committee affirmed the adoption of the going concern assumption to prepare the accounts.

- **External audit**
  The Committee considered matters raised during the statutory external audit and concluded that there were no adjustments required which were material to the financial statements.

b) Risk and internal control

The Society recognises the importance of effective risk management and strong systems of internal control in the achievement of its objectives and the safeguarding of its assets, and also facilitates the effectiveness and efficiency of operations, which help to ensure the reliability of internal and external reporting and assist in compliance with applicable laws and regulations. The Society operates in a dynamic business environment and, as a result, the risks it faces change continually. Management are responsible for designing the internal control framework to ensure thorough and regular evaluation of the nature and extent of risk and the Society's ability to react accordingly. Management are also responsible for implementing the Board's policies on risk and control, noting that all employees are responsible for internal control as part of their individual objectives.

Further details of actual risk management practices are provided in the Risk Management Report on pages 23 to 27. Through the Committee, the Society's Internal Audit function provides independent assurance to the Board on the effectiveness of the internal control framework. The information received and considered by the Committee during the 2016/17 financial year provided reasonable assurance that there were no material breaches of control and that, overall, the Society maintained an adequate internal control framework that met the principles of the UK Corporate Governance Code.

Internal Audit utilise the services of external specialists for support in providing assurance in technical areas, primarily, Information Technology, Treasury and Credit Risk. The Divisional Director Internal Audit reports to the Chairman of the Committee, and the Committee is responsible for agreeing the annual budget for Internal Audit, in addition to ensuring that the function retains adequate skills and resource levels that are sufficient to provide the level of assurance required.

The Audit Committee approves the Internal Audit plan of work, including subsequent amendments, which is prepared on a risk based approach by Internal Audit and reflects input from management and the Committee. The Committee reviews the work of, and output from, Internal Audit, in addition to progress against the agreed plan of work. Internal Audit provides the Committee with reports on material findings and recommendations and updates on the progress made by management in addressing those findings.

The Committee also reviews periodically the use of the confidential reporting channel in the Society. Awareness of 'whistle blowing' arrangements is maintained through internal communication and is covered as part of employees' induction and ongoing development.

As part of the external audit process, the external auditor provides internal control reports. During the year, KPMG LLP did not highlight any material control weaknesses.

The Committee recommends an external 'effectiveness review' of Internal Audit every three years. A review was carried out during the 2013/14 financial year by an external firm appointed by the Committee. In performing their review, information was gathered from a variety of sources including interviews with key business stakeholders, workshops with the Internal Audit team, and a review of key documentation covering all aspects of the Internal Audit function (including file reviews). An external assessment of Internal Audit's readiness to comply with the Chartered Institute of Internal Auditors recommendations on 'Effective Internal Audit in the Financial Services sector', issued in July 2013, was also included.

The review concluded that the Internal Audit function is operating effectively in providing assurance to the Committee and a wide range of key stakeholders.

c) External auditor

KPMG, as KPMG Audit Plc, and since 29 July 2014 as KPMG LLP, has been the Society's auditor since 1993.

The Committee regularly monitors the Society's relationship with the external auditor and has adopted a framework for ensuring auditor independence and objectivity, which defines unacceptable non-audit assignments, pre-approval of acceptable non-audit assignments and procedures for approval of other non-audit assignments across the Society.

Details of the fees paid to the external auditor for audit and non-audit services are set out in note 6 to the Accounts.
The Committee has also agreed a policy for the employment, by the Society, of former employees of the external auditor which is designed to further maintain the auditor's independence.

The Committee assesses the effectiveness of the external auditor annually, immediately after the completion of their year-end audit, the results of which are reported to and discussed at the next appropriate Committee meeting. This assessment is facilitated by the Group Secretary and is discussed, initially, without the presence of the auditor in the meeting.
The Committee considers that the relationship with the auditor is working well and is satisfied with their effectiveness and independence.

Audit Committee effectiveness

The effectiveness of the Committee was assessed by an external firm in July 2013. The scope of this review considered time management and composition, Committee processes and support, the work of the Committee and future priorities.
This review concluded that the Committee operated effectively, being highly rated in each of the areas reviewed.

Committee members are expected to undertake relevant training as part of their ongoing development and, periodically, the Committee as a whole receives training on current topics.

On behalf of the Board

Colin Walklin
Chairman of Audit Committee
30 May 2017

Directors' Remuneration Report

Annual Statement by the Chairman of the Remuneration Committee

I am pleased to present the Directors' Remuneration Report which sets out details of pay, benefits and performance-related pay for Directors.

The Remuneration Committee has decided to adopt voluntarily the relevant requirements of the UK Corporate Governance Code, in so far as they are considered appropriate for a building society. The tables marked 'audited' in this report are requirements of the Building Societies Act 1986. The report also complies with the third EU Capital Requirements Directive and the detailed requirements of the Financial Conduct Authority's (FCA's) Remuneration Code (the Code). Details of the Code can be found at www.fca.org.uk.

Under the Code, the Society is required to identify those staff who are considered to have a material impact on the Society's risk profile (Code Staff). This includes all Executive and Non-Executive Directors and all members of the Society's Executive Committee (ExCo).

This report is presented in two sections:

- The Remuneration Policy – setting out the Remuneration Committee's forward-looking policy with regard to pay and benefits. It is the Committee's intention that this policy will apply with effect from the Annual General Meeting (AGM), following an advisory vote by members. The only material change introduced during the financial year 2016/17 was the introduction of a provision allowing the Society to 'claw back' performance-related pay awards for a period of up to three years after they were awarded. The Society is not required to make this change, but wishes to do so in order to be at the forefront of good corporate governance. This provision applies to performance-related awards made from 2016 onwards. The Remuneration Policy, if unchanged, is voted on every three years.
- The Annual Remuneration Report – detailing the amounts earned by Directors in respect of the financial year ended 31 March 2017 and how the policy will operate for the year ending 31 March 2018.

All eligible members receive a copy of the Remuneration Report and are entitled to participate in advisory votes on both the Remuneration Policy and the Annual Remuneration Report at the 2017 AGM.

As reported in the Chief Executive's Review, notwithstanding the statutory loss before tax of £19.8m, the Society performed strongly in 2016/17 with underlying profitability up 60% to £7.7m. New residential lending of £712m contributed to a 15% increase in the prime owner occupied book, while the Society's exposure to riskier commercial lending continued to reduce, down 14% year on year.

On 31 March 2016 Mr Gibbard informed the Board of his intention to retire on 31 March 2017. Mr Gibbard subsequently submitted his formal notice and worked as Group Finance & Operations Director until 13 March 2017 and as a Board member until 31 March 2017.

Mr Ashraf Piranie took up the role as Group Finance & Operations Director as of 13 March 2017. The package offered to Mr Piranie was in line with that outlined in the Remuneration Policy. In accordance with this Policy, the Board agreed to compensate Mr Piranie, who was required to forego an element of his performance-related pay awards from his previous employer. This compensation will replicate, as far as possible, the amount and terms that he would have received had he stayed in post. The maximum exposure to the sum payable to Mr Piranie is £161,000.

For the financial year 2016/17 both Executive Directors received a pay increase of 2%, staff also received a 2% increase on 1 April 2016. On 1 April 2017 the Chief Executive received an increase of 2%, again matching the general increase given to staff.

The Executive Director Performance-Related Pay Award payable to the Chief Executive and Group Finance & Operations Director (Mr Gibbard) generated awards of between 38.4% and 43.5% of salary. These payments reflect the delivery of financial measures, the management of risk, both credit risk and operational risk, customer and people measures and new and enhanced operational capabilities. As referred to in the Chairman's Statement, with respect to the variation of interest charged on certain buy to let loans, at no time were the Executive Directors incentivised or rewarded on the basis of the increase applied, and accordingly their remuneration is unaffected by the reversal of the initial High Court decision and the subsequent refund of interest.

Deferred performance-related payments in relation to 2013/14, 2014/15 and 2015/16 for Executive Directors have been approved for payment since the end of the 2016/17 financial year.

Fees for the Chairman and other Non-Executive Directors were reviewed for the 2016/17 financial year and no increases were applied. A further review for the 2017/18 financial year also resulted in no increase in fees for the Chairman or any Non-Executive Director.

Martin Ritchley
Chairman of Remuneration Committee
30 May 2017

Remuneration Committee membership and responsibilities

Membership

The members of the Remuneration Committee during the financial year 2016/17 were: Martin Ritchley, Mark Nicholls, Claire Hafner and Mark Preston.

All members of the Committee are Non-Executive Directors. Under the Committee's terms of reference, at least one member of the Committee must also be a member of either the Risk Committee or Audit Committee. The current composition of the Committee complies with this requirement.

The Society's Chief Executive, Group Finance & Operations Director, Group Secretary and Divisional Director Human Resources attend meetings by invitation.

Responsibilities

The Committee is responsible for setting the policy on remuneration, overseeing its implementation and making recommendations to the Board in respect of remuneration arrangements for Executive Directors and other Code Staff.

Following each meeting, the Chairman of the Committee reports to the Board on all substantive issues discussed.

The Committee is required to meet at least twice a year. During the year there were six meetings.

The Committee considered the following matters during the year:

- Determining the pay and benefits of Executive Directors, the Chairman, Code Staff and other senior managers and recommending to the Board for approval;
- Determining the pay and benefits for the new Group Finance & Operations Director and recommending for Board approval;
- Determining the pay and benefits for staff;
- Determining the level of performance-related pay in relation to the 2015/16 financial year and deferred awards due during the year for Code Staff and recommending to the Board for approval;
- Recommending to the Board the Society and individual performance-related pay objectives for Code Staff in relation to the 2017/18 financial year;
- Considering the approach to be adopted in respect of disclosure requirements in relation to this report; and
- Considering the approach for the forthcoming Gender Pay Regulations.

The Committee receives an annual report, prepared jointly by the Group Secretary, Chief Financial Risk Officer and the Divisional Director Internal Audit. This report provides information on whether any activity or behaviour by any individual has been identified or observed which should affect their eligibility to participate in performance-related pay arrangements. No such behaviours were reported.

No member, or invitee, is present when their own remuneration is discussed.

The Terms of Reference for the Committee were last updated in March 2017. The Terms of Reference are available on request from the Group Secretary.

Advisors

Where required the Remuneration Committee will use the services of Deloitte LLP to provide independent advice on executive remuneration. Deloitte is a founding member of the Remuneration Consulting Group and as such voluntarily operating under the Code of Conduct in relation to the executive remuneration consulting.

Section 1 – The Remuneration Policy

Background

The Remuneration Policy (the Policy) provides the framework for the Committee to make remuneration decisions in relation to Executive Directors and other Code Staff.

The Policy is designed to promote appropriate behaviours and is aligned with the Society's risk appetite.

The approach of the Remuneration Committee is to ensure that Executive Directors' remuneration is designed to promote the long-term success of the Society, with full consideration of other stakeholders such as members and regulators.

Remuneration decisions are made on the basis of total compensation comprising salary, performance-related pay and benefits, ensuring an appropriate balance between the fixed and variable components of remuneration. The variable element of the remuneration package creates flexibility to allow for changes in current and future performance.

The Society's remuneration principles are as follows:

- The Policy is in line with the strategy, objectives and values of the Society, thereby aligning it with both short and long-term interests;
- The policies, procedures, remuneration practices and performance-related payment schemes are consistent with the promotion of good and effective risk management and are structured in such a way as to discourage risk taking which is outside the Society's risk appetite;
- The Society's focus is on improving the underlying business position where management can influence performance. The Society's performance-related pay schemes may therefore exclude the impact of specific one-off items which would be agreed at the outset by the Society's Board following a recommendation by the Remuneration Committee;
- All remuneration packages are designed such that the Society can attract and retain high calibre individuals;
- Performance measures for individuals are challenging and robust and measured on a consistent basis; and
- Performance-related pay is performance dependent, an element of which is deferred over a three year period, to allow the Remuneration Committee to review whether the payment remains appropriate, and providing the ability to reduce or cancel the payment.

The Policy follows, as a minimum, regulatory requirements and good corporate governance practices.

Remuneration policy and practice

Components of remuneration

The table below describes the Society's policy with respect to each element of pay for Executive Directors:

Component	Operation and performance metrics	Opportunity
Basic salary Fixed remuneration set to attract and retain Executives of sufficient calibre through the payment of competitive rates.	Reviewed annually (or more frequently if required). Influencing factors include: role and experience, personal performance, benchmarking comparisons and salary increases awarded across the Society.	Set at a level considered appropriate, taking into account the relevant factors tabled. The Committee considers very carefully any pay awards which do not reflect the wider increases across the Society and will only make them where there is a clear commercial rationale for doing so.
Performance-related pay Linked to the delivery of Society and personal objectives. Used to reward Executive Directors within the context of achieving the Society's goals and objectives.	40% of the performance-related pay earned (maximum 20% of basic salary) is deferred over a three year period. Deferred payments are made in equal instalments over the following three years, are subject to annual review and recommendation by the Committee and require approval by the Non-Executive members of the Board. The Committee has discretion to adjust or recover awards if necessary including withholding vested awards (malus arrangements) and recovering payments (clawback arrangements). All awards are non-pensionable. Based on a number of measures, including: financial, customer, people, risk and new and enhanced operational capabilities. Reviewed by the Committee annually to ensure that the measures are appropriate.	Maximum annual opportunity is 50% of basic salary.
Pension or pension allowance A part of fixed remuneration intended to attract and retain Executive Directors of sufficient calibre.	Executive Directors are invited to join the Society's stakeholder pension plan or, as an alternative, be provided with a cash allowance.	A cash allowance of up to 25% of basic salary for the Executive Directors.
Benefits A part of fixed remuneration intended to attract and retain Executive Directors of sufficient calibre.	Executive Directors receive benefits in line with market practice, which include a fully expensed car or cash allowance, private medical care for themselves and their family, and life assurance. Other benefits may be provided in individual circumstances.	Set at a level considered appropriate by the Committee.

The table below shows the policy for Non-Executive Directors:

Component	Operation	Application
Fees To attract and retain Non-Executive Directors of the right calibre for the Society.	Fees are reviewed annually for Non-Executive Directors by the Chairman and Executive Directors. Fees for the Chairman are recommended by the Remuneration Committee and approved by the Board. The Chairman is not present when his fees are discussed or approved.	Fees are set at a level to attract individuals with the appropriate knowledge and experience and to reflect the responsibilities and time commitment for Board and Board Committees, taking into account market practice.

Whilst Non-Executive Directors do not participate in any performance-related pay scheme, their overall performance is reviewed annually by the Chairman.

Recruitment policy for Executive Directors

The appointment of an Executive Director could be either an internal or external appointment. In principle, the Society would look to provide no additional benefits to a new Director than those provided to an existing Director.

The Committee's approach is to offer a package that is sufficient to recruit an individual of sufficient calibre, but to pay no more than is necessary to attract the appropriate candidate.

Component	Application
Basic salary	A Director would receive an amount commensurate with their experience and responsibilities.
Benefits	A Director would receive comparable benefits to existing Directors, although if required to attract the right candidate these may be widened to include additional benefits, such as a relocation allowance.
Performance-related pay	The maximum performance-related award would be in line with current policy, unless the market rate required to recruit the individual supported a higher amount. In any event, this would be no more than what is considered commercially justifiable.
Pension or pension allowance	A Director would have the option to join the Society's stakeholder pension scheme or to receive a cash allowance of up to 25% of salary.
Recruitment compensation	Compensation arrangements are only considered if the new Director was required to forego an arrangement from their previous employer. In such instances the award would be no more in terms of amount than the award due to be forgone. The timing and vesting requirements of any payment would be replicated as far as possible.

The Committee has discretion within the Policy to make remuneration decisions where it considers it necessary to do so. In setting remuneration arrangements for new hires, the Committee will consider the value of the package on offer compared to similar positions in the market, the structure of the remuneration and the experience of the candidate, to ensure that arrangements are in the best interests of both the Society and its members, without paying in excess of what is deemed necessary to recruit a Director of the required calibre.

Recruitment policy for Non-Executive Directors

As with Executive Directors, the Committee's approach is to offer a package that is sufficient to recruit an individual of sufficient calibre, but to pay no more than is necessary to attract the appropriate candidate.

Component	Application
Fees	A new Non-Executive Director would receive fees. The level of fees would be set at a level commensurate with their experience and responsibilities and with due regard to the fees of other Non-Executive Directors.

Service contracts

The terms and conditions of employment for Executive Directors are detailed in their service contracts. The contract is terminable with twelve months' notice if given by the Society or six months' notice if given by the Director.

Non-Executive Directors do not have service contracts and instead have letters of engagement which set out their time commitments and responsibilities.

Policy on payment for loss of office

The Committee's approach is to pay no more than is necessary in such circumstances. Since 2012, the Society's policy is for new contracts to require Executive Directors to mitigate their loss in the event of receiving a 'loss of office' payment.

Component	Application
Salary and benefits	A termination payment would be on the basis of the relevant notice period. There would be no payment in the event of misconduct or poor performance.
Performance-related pay	Any performance-related pay awards would be made solely at the discretion of the Committee. Any deferred awards would remain payable in future years subject to the normal rules of the Scheme, including possible reduction or cancellation.

Section 1 – The Remuneration Policy (continued)

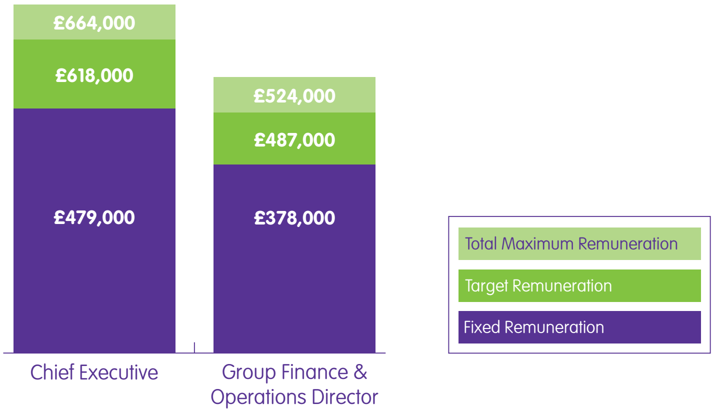
Employment conditions elsewhere in the Society

The pay and benefits of staff are considered annually by the Committee, which also determines the amount of general performance-related pay. The Society, subject to eligibility, offers a comprehensive range of benefits to staff, including pension, life assurance, health care and performance-related pay.

Remuneration scenarios

The following charts show the breakdown of the component parts of the remuneration package for Executive Directors for 2016/17 on the following basis:

- Fixed remuneration - comprising of basic salary, pension and benefits.
- Target remuneration - the anticipated annual remuneration incorporating a performance-related award.
- Maximum remuneration - the maximum remuneration that could be awarded.



When developing the scenarios, the following assumptions were made:

- Fixed remuneration includes basic salary, pension and benefits only;
- Target remuneration is based on a performance-related award of 37.5% of basic salary; and
- Maximum award is based on a performance-related award of the maximum achievable which is 50% of basic salary.

Section 2 – Annual Report on Remuneration

Non-Executive Director fees (audited)

Non-Executive Director	Date appointed	2016/17 Fees £000	2016/17 Benefits (1) £000	2015/16 Fees £000	2015/16 Benefits (1) £000
Mark Nicholls (Society Chairman)	01/01/10	**120**	**5**	120	5
Claire Hafner	01/09/11	**50**	**5**	50	5
Julie Hopes	01/04/16	**50**	**5**	-	-
Mark Preston	18/05/11	**50**	**4**	50	5
Martin Ritchley (Deputy Chairman & Remuneration Committee Chairman)	01/09/09	**70**	**2**	70	3
Richard Sommers (Risk Committee Chairman)	01/10/09	**60**	**6**	60	3
Colin Walklin (Audit Committee Chairman)	20/07/11	**60**	**5**	60	6
Total		**460**	**32**	410	27

Notes:
1. In addition to the payment of fees, Non-Executive Directors receive expenses for travel and accommodation in relation to their attendance at meetings.

Executive Director remuneration – 2016/17 (audited)

Executive Director		Basic salary £000	Performance-related pay (1) £000	Pension £000	Other benefits £000	Total £000
Jonathan Westhoff	(Chief Executive)	370	142	93	26(2)	**631**
Ashraf Piranie	(Group Finance & Operations Director from 13 March 2017)	16	-	4	1	**21**
Mark Gibbard(3)	(Group Finance & Operations Director to 13 March 2017)	291	126	58	29	**504**
Total		**677**	**268**	**155**	**56**	**1,156**

Executive Director remuneration – 2015/16 (audited)

Executive Director		Basic salary £000	Performance-related pay (1) £000	Pension £000	Other benefits £000	Total £000
Jonathan Westhoff	(Chief Executive)	363	150	91	32	636
Mark Gibbard	(Group Finance & Operations Director)	285	119	57	30	491
Total		648	269	148	62	1,127

Notes:
1. Included in the amounts shown above is an element that is subject to deferral. The table overleaf headed 'Executive Director deferred performance-related pay payable in future years' details the amount due for payment, subject to review by the Committee at the appropriate time.
2. Mr Westhoff received compensation of £10,000 relating to travel costs for a holiday which he was required to cancel at short notice to fulfil his role, and reflects a proportion of the non-recoverable costs of cancellation.
3. In March 2016 Mr Gibbard informed the Board of his intention to retire on 31 March 2017. Mr Gibbard worked his full notice period, he handed over his role of Group Finance & Operations Director on 13 March 2017 and retired from the Board on 31 March 2017. Other than deferred performance-related pay awards which may become payable in future years (as described overleaf) there are no further payments due to him.

Section 2 – Annual Report on Remuneration (continued)

A proportion of the Executive Directors' performance-related pay has been deferred as shown in the table below. Payment of any deferred award is subject to review by the Remuneration Committee and approval by the Board, and may be reduced or cancelled as appropriate.

Executive Director deferred performance-related pay
Payable in future years

Executive Director	Deferred from	Payable after year ending 2016/17 £000	2017/18 £000	2018/19 £000	2019/20 £000
Jonathan Westhoff	2013/14	18	-	-	-
	2014/15	20	20	-	-
	2015/16	20	20	20	-
	2016/17	-	19	19	19
Total		**58**	**59**	**39**	**19**
Mark Gibbard	2013/14	15	-	-	-
	2014/15	16	16	-	-
	2015/16	16	16	16	-
	2016/17	-	17	17	17
Total		**47**	**49**	**33**	**17**
Andrew Jones	2013/14	9	-	-	-
Total		**9**	**-**	**-**	**-**

Deferred elements due after the year ending 2016/17 (shown in the table above) have subsequently been approved by the Board for payment.

Statement on member voting at the 2016 AGM

At the 2016 AGM members voted in favour of approving the Directors' Remuneration Report as shown below:

Vote	Votes for	% of votes	Votes against	Withheld*
To approve the Directors' Remuneration Report	19,261	90.21%	2,091	452

* The withheld figures are not included in the calculation of % 'Votes for'.

The Remuneration Policy for 2017/18

The Remuneration Committee is required annually to review the salaries of the Executive Directors. A recommendation was made by the Remuneration Committee and subsequently approved by the Board, to increase the basic annual salary of the Chief Executive from £370,260 to £377,665 from 1 April 2017, representing a 2% award.

The annual salary review for staff, which provided an increase of 2%, was applied from 1 April 2017.

The Remuneration Committee has decided that it will undertake a benchmarking exercise of all Director remuneration to include the Executive Directors, Non-Executive Directors and the Chairman during the 2017/18 financial year.

The maximum performance-related pay award for Executive Directors will remain at 50% of salary for 2017/18.

The Remuneration Committee will continue to strive to align its decisions with industry best practice and regulatory requirements whilst considering both the best interests of the Society and the interests of members.

Martin Ritchley
Chairman of Remuneration Committee
30 May 2017

Independent Auditor's Report

Independent auditor's report to the members of West Bromwich Building Society

We have audited the Group and Society Annual Accounts of West Bromwich Building Society for the year ended 31 March 2017 set out on pages 48 to 110. The financial reporting framework that has been applied in their preparation is applicable law and International Financial Reporting Standards (IFRSs) as adopted by the EU.

This report is made solely to the Society's members, as a body, in accordance with section 78 of the Building Societies Act 1986. Our audit work has been undertaken so that we might state to the Society's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Society and the Society's members as a body, for our audit work, for this report, or for the opinions we have formed.

Respective responsibilities of Directors and Auditor

As explained more fully in the Directors' Responsibilities Statement set out on pages 31 to 32, the Directors are responsible for the preparation of Annual Accounts which give a true and fair view. Our responsibility is to audit, and express an opinion on, the Annual Accounts in accordance with applicable law and International Standards on Auditing (UK and Ireland). Those standards require us to comply with the Auditing Practices Board's Ethical Standards for Auditors.

Scope of the audit of the Annual Accounts

A description of the scope of an audit of financial statements is provided on the Financial Reporting Council's website at www.frc.org.uk/auditscopeukprivate.

Opinion on Annual Accounts

In our opinion the Annual Accounts:

- give a true and fair view, in accordance with IFRSs as adopted by the EU, of the state of affairs of the Group and of the Society as at 31 March 2017 and of the income and expenditure of the Group and of the Society for the year then ended; and
- have been prepared in accordance with the requirements of the Building Societies Act 1986 and regulations made under it and, as regards the Group Annual Accounts, Article 4 of the IAS Regulation.

Opinion on other matters prescribed by the Building Societies Act 1986

In our opinion:

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

Matters on which we are required to report by exception

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

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

Jonathan Holt (Senior Statutory Auditor)
for and on behalf of KPMG LLP, Statutory Auditor
Chartered Accountants
One Snowhill
Snow Hill Queensway
Birmingham
B4 6GH
30 May 2017

Income Statements

for the year ended 31 March 2017

	Notes	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Interest receivable and similar income	2	108.9	126.7	103.8	118.0
Interest expense and similar charges	3	(53.6)	(66.7)	(53.5)	(67.4)
Net interest receivable		55.3	60.0	50.3	50.6
Fees and commissions receivable		2.7	3.7	2.9	3.8
Other operating income	4	4.1	3.9	37.4	30.5
Total operating income		62.1	67.6	90.6	84.9
Fair value losses on financial instruments		(0.2)	(1.0)	(0.6)	(1.6)
Net realised profits	5	0.5	0.6	0.5	0.6
Total income		62.4	67.2	90.5	83.9
Administrative expenses	6	(44.4)	(42.0)	(40.4)	(37.8)
Depreciation and amortisation	16,18	(5.7)	(5.1)	(5.7)	(5.1)
Operating profit before revaluation gains, impairment and provisions		12.3	20.1	44.4	41.0
Gains on investment properties	17	5.4	5.5	-	-
Impairment on loans and advances	14	(7.6)	(8.1)	1.2	1.6
Provisions for liabilities	25	(29.9)	(4.0)	(2.3)	(4.0)
Provisions against investments in subsidiary undertakings	15	-	-	(37.5)	(30.8)
(Loss)/Profit before tax		(19.8)	13.5	5.8	7.8
Taxation	9	(6.0)	(4.1)	(3.0)	0.3
(Loss)/Profit for the financial year		(25.8)	9.4	2.8	8.1

The (loss)/profit for the year derives wholly from continuing operations.

The notes on pages 55 to 110 form part of these accounts.

Statements of Comprehensive Income

for the year ended 31 March 2017

	Notes	Group 2017 £m	Group 2016 £m
(Loss)/Profit for the financial year		**(25.8)**	9.4
Other comprehensive income			
Items that may subsequently be reclassified to profit or loss			
Available for sale investments			
Valuation gains/(losses) taken to equity		**0.5**	(2.2)
Amounts transferred to Income Statement		**(0.5)**	(0.6)
Cash flow hedge losses taken to equity		**(0.5)**	(0.2)
Taxation	29	**0.1**	0.2
Items that will not subsequently be reclassified to profit or loss			
Gains on revaluation of land and buildings		**0.6**	-
Actuarial losses on defined benefit obligations	30	**(10.4)**	(0.9)
Amortisation of original discount on subscribed capital		**0.1**	-
Taxation	29	**1.7**	0.1
Other comprehensive income for the financial year, net of tax		**(8.4)**	(3.6)
Total comprehensive income for the financial year		**(34.2)**	5.8

	Notes	Society 2017 £m	Society 2016 £m
Profit for the financial year		**2.8**	8.1
Other comprehensive income			
Items that may subsequently be reclassified to profit or loss			
Available for sale investments			
Valuation gains/(losses) taken to equity		**0.5**	(2.2)
Amounts transferred to Income Statement		**(0.5)**	(0.6)
Taxation	29	**-**	0.2
Items that will not subsequently be reclassified to profit or loss			
Gains on revaluation of land and buildings		**0.6**	-
Actuarial losses on defined benefit obligations	30	**(10.4)**	(0.9)
Amortisation of original discount on subscribed capital		**0.1**	-
Taxation	29	**1.7**	0.1
Other comprehensive income for the financial year, net of tax		**(8.0)**	(3.4)
Total comprehensive income for the financial year		**(5.2)**	4.7

The notes on pages 55 to 110 form part of these accounts.

Statements of Financial Position

at 31 March 2017

	Notes	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Assets					
Cash and balances with the Bank of England	10	**294.8**	215.4	**294.8**	215.4
Loans and advances to credit institutions		**174.0**	204.0	**91.7**	93.2
Investment securities	11	**385.0**	410.1	**1,195.5**	1,300.0
Derivative financial instruments	12	**6.3**	8.9	**6.2**	8.8
Loans and advances to customers	13	**4,776.5**	4,739.0	**2,663.7**	2,380.1
Deferred tax assets	19	**16.4**	20.4	**11.7**	13.5
Trade and other receivables	20	**3.5**	2.7	**3.3**	2.7
Investments	15	**-**	-	**1,526.9**	1,669.2
Intangible assets	16	**13.3**	8.2	**12.7**	7.6
Investment properties	17	**128.9**	123.7	**-**	-
Property, plant and equipment	18	**32.1**	33.9	**32.1**	33.9
Retirement benefit assets	30	**-**	0.8	**-**	0.8
Total assets		**5,830.8**	5,767.1	**5,838.6**	5,725.2
Liabilities					
Shares	21	**4,427.3**	4,385.1	**4,427.3**	4,385.1
Amounts due to credit institutions		**450.3**	259.0	**450.3**	259.0
Amounts due to other customers	22	**132.7**	157.0	**390.3**	500.0
Derivative financial instruments	12	**69.0**	77.1	**59.7**	67.4
Debt securities in issue	23	**263.2**	368.6	**-**	-
Deferred tax liabilities	19	**5.0**	4.7	**1.0**	0.6
Trade and other payables	24	**10.2**	15.2	**9.4**	14.2
Provisions for liabilities	25	**3.1**	2.7	**3.0**	2.6
Retirement benefit obligations	30	**6.5**	-	**6.5**	-
Total liabilities		**5,367.3**	5,269.4	**5,347.5**	5,228.9
Equity					
Profit participating deferred shares	27	**173.0**	179.5	**173.0**	179.5
Subscribed capital	26	**75.0**	74.9	**75.0**	74.9
General reserves		**211.0**	239.3	**237.9**	237.6
Revaluation reserve		**3.5**	3.4	**3.5**	3.4
Available for sale reserve		**1.7**	0.9	**1.7**	0.9
Cash flow hedging reserve		**(0.7)**	(0.3)	**-**	-
Total equity attributable to members		**463.5**	497.7	**491.1**	496.3
Total liabilities and equity		**5,830.8**	5,767.1	**5,838.6**	5,725.2

The accounting policies and notes on pages 55 to 110 form part of these accounts.

Approved by the Board of Directors on 30 May 2017 and signed on its behalf by:

Mark Nicholls
Chairman

Jonathan Westhoff
Chief Executive

Ashraf Piranie
Group Finance & Operations Director

Statements of Changes in Members' Interest

for the year ended 31 March 2017

Group	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2016	**179.5**	**74.9**	**239.3**	**3.4**	**0.9**	**(0.3)**	**497.7**
Loss for the financial year	(6.5)	-	(19.3)	-	-	-	**(25.8)**
Other comprehensive income for the period							
Amortisation of original discount on subscribed capital	-	0.1	-	-	-	-	**0.1**
Available for sale investments: reallocation of tax*	-	-	(0.8)	-	0.8	-	**-**
Actuarial losses on defined benefit obligations	-	-	(8.5)	-	-	-	**(8.5)**
Gains on revaluation of land and buildings	-	-	-	0.4	-	-	**0.4**
Realisation of previous revaluation gains	-	-	0.3	(0.3)	-	-	**-**
Cash flow hedge losses	-	-	-	-	-	(0.4)	**(0.4)**
Total other comprehensive income	**-**	**0.1**	**(9.0)**	**0.1**	**0.8**	**(0.4)**	**(8.4)**
Total comprehensive income for the year	**(6.5)**	**0.1**	**(28.3)**	**0.1**	**0.8**	**(0.4)**	**(34.2)**
At 31 March 2017	**173.0**	**75.0**	**211.0**	**3.5**	**1.7**	**(0.7)**	**463.5**

for the year ended 31 March 2016

Group	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Cash flow hedging reserve £m	Total £m
At 1 April 2015	177.1	74.9	233.1	3.4	3.5	(0.1)	491.9
Profit for the financial year	2.4	-	7.0	-	-	-	9.4
Other comprehensive income for the period							
Available for sale investments: current year movement net of tax	-	-	-	-	(2.6)	-	(2.6)
Actuarial losses on defined benefit obligations	-	-	(0.8)	-	-	-	(0.8)
Cash flow hedge losses	-	-	-	-	-	(0.2)	(0.2)
Total other comprehensive income	-	-	(0.8)	-	(2.6)	(0.2)	(3.6)
Total comprehensive income for the year	2.4	-	6.2	-	(2.6)	(0.2)	5.8
At 31 March 2016	179.5	74.9	239.3	3.4	0.9	(0.3)	497.7

Statements of Changes in Members' Interest

for the year ended 31 March 2017

Society	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Total £m
At 1 April 2016	**179.5**	**74.9**	**237.6**	**3.4**	**0.9**	**496.3**
(Loss)/Profit for the financial year	(6.5)	-	9.3	-	-	**2.8**
Other comprehensive income for the period						
Amortisation of original discount on subscribed capital	-	0.1	-	-	-	**0.1**
Available for sale investments: reallocation of tax*	-	-	(0.8)	-	0.8	**-**
Actuarial losses on defined benefit obligations	-	-	(8.5)	-	-	**(8.5)**
Gains on revaluation of land and buildings	-	-	-	0.4	-	**0.4**
Realisation of previous revaluation gains	-	-	0.3	(0.3)	-	**-**
Total other comprehensive income	**-**	**0.1**	**(9.0)**	**0.1**	**0.8**	**(8.0)**
Total comprehensive income for the year	**(6.5)**	**0.1**	**0.3**	**0.1**	**0.8**	**(5.2)**
At 31 March 2017	**173.0**	**75.0**	**237.9**	**3.5**	**1.7**	**491.1**

for the year ended 31 March 2016

Society	Profit participating deferred shares £m	Subscribed capital £m	General reserves £m	Revaluation reserve £m	Available for sale reserve £m	Total £m
At 1 April 2015	177.1	74.9	232.7	3.4	3.5	491.6
Profit for the financial year	2.4	-	5.7	-	-	8.1
Other comprehensive income for the period						
Available for sale investments: current year movement net of tax	-	-	-	-	(2.6)	(2.6)
Actuarial losses on defined benefit obligations	-	-	(0.8)	-	-	(0.8)
Total other comprehensive income	-	-	(0.8)	-	(2.6)	(3.4)
Total comprehensive income for the year	2.4	-	4.9	-	(2.6)	4.7
At 31 March 2016	179.5	74.9	237.6	3.4	0.9	496.3

*Tax in relation to available for sale investments has been reallocated to reflect the underlying transactions.

Under the terms of the profit participating deferred shares (PPDS), 25% of the annual post-tax profits or (losses) are allocated against the PPDS reserve.

The notes on pages 55 to 110 form part of these accounts.

Statements of Cash Flows

for the year ended 31 March 2017

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Net cash inflow/(outflow) from operating activities (below)	**138.7**	220.3	**(123.7)**	(191.5)
Cash flows from investing activities				
Purchase of investment securities	**(230.4)**	(386.7)	**(230.4)**	(386.7)
Proceeds from disposal of investment securities	**213.1**	298.0	**345.2**	403.9
Proceeds from disposal of investment properties	**0.2**	0.4	**-**	-
Purchase of property, plant and equipment and intangible assets	**(9.6)**	(8.8)	**(9.6)**	(8.8)
Proceeds from disposal of property, plant and equipment	**0.5**	-	**0.5**	-
New funding to subsidiaries	**-**	-	**(145.1)**	(151.2)
Dividends received	**-**	-	**37.5**	30.7
Repayment of funding from subsidiaries	**-**	-	**213.3**	321.9
Net cash flows from investing activities	**(26.2)**	(97.1)	**211.4**	209.8
Cash flows from financing activities				
Repayment of mortgage backed loan notes	**(106.0)**	(98.5)	**-**	-
Net cash flows from financing activities	**(106.0)**	(98.5)	**-**	-
Net increase in cash	**6.5**	24.7	**87.7**	18.3
Cash and cash equivalents at beginning of year	**468.8**	444.1	**358.0**	339.7
Cash and cash equivalents at end of year	**475.3**	468.8	**445.7**	358.0

For the purposes of the statements of cash flows, cash and cash equivalents comprise the following balances with less than 90 days maturity:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Cash in hand (including Bank of England Reserve account)	**287.6**	208.7	**287.6**	208.7
Loans and advances to credit institutions	**174.0**	204.0	**91.7**	93.2
Investment securities	**13.7**	56.1	**66.4**	56.1
	475.3	468.8	**445.7**	358.0

The Group is required to maintain certain mandatory balances with the Bank of England which, at 31 March 2017, amounted to £7.2m (2015/16: £6.7m).
The movement in these balances is included within cash flows from operating activities.

Statements of Cash Flows (continued)

for the year ended 31 March 2017

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Cash flows from operating activities				
(Loss)/Profit on ordinary activities before tax from continuing activities	**(19.8)**	13.5	**5.8**	7.8
Movement in prepayments and accrued income	**(0.8)**	(0.2)	**(0.8)**	(0.2)
Movement in accruals and deferred income	**(2.6)**	(0.4)	**(2.9)**	(0.3)
Impairment on loans and advances	**7.6**	8.1	**(1.2)**	(1.6)
Depreciation and amortisation	**5.7**	5.1	**5.7**	5.1
Revaluations of investment properties	**(5.4)**	(5.5)	**-**	-
Movement in provisions for liabilities	**0.4**	0.5	**0.4**	0.7
Movement in provisions against investments in subsidiary undertakings	**-**	-	**37.5**	30.8
Movement in derivative financial instruments	**(5.5)**	6.4	**(5.1)**	8.6
Movement in fair value adjustments	**(0.7)**	(2.3)	**(5.5)**	(11.6)
Movement in subscribed capital	**0.1**	-	**0.1**	-
Change in retirement benefit obligations	**(3.1)**	(9.2)	**(3.1)**	(9.2)
Cash flows from operating activities before changes in operating assets and liabilities	**(24.1)**	16.0	**30.9**	30.1
Movement in loans and advances to customers	**(47.7)**	(72.4)	**(280.3)**	(387.3)
Movement in loans and advances to credit institutions	**(0.5)**	0.6	**(0.5)**	0.5
Movement in shares	**45.7**	407.1	**45.7**	407.1
Movement in deposits and other borrowings	**167.0**	(129.7)	**81.6**	(240.7)
Movement in trade and other receivables	**-**	2.4	**0.2**	(1.9)
Movement in trade and other payables	**(1.7)**	(3.7)	**(1.3)**	0.7
Net cash inflow/(outflow) from operating activities	**138.7**	220.3	**(123.7)**	(191.5)

The notes on pages 55 to 110 form part of these accounts.

Notes to the Accounts

1. Accounting policies

The principal accounting policies applied consistently in the preparation of these consolidated Annual Accounts are set out below.

Basis of preparation

The Annual Accounts of the Group and the Society have been prepared in accordance with International Financial Reporting Standards (IFRS) and its interpretations as adopted by the European Union (EU) and effective at 31 March 2017; and with those parts of the Building Societies (Accounts and Related Provisions) Regulations 1998 and the Building Societies Act 1986 applicable to societies reporting under IFRS.

The Annual Accounts have been prepared under the historical cost convention as modified by the revaluation of available for sale assets, derivatives, investment properties, property, plant and equipment and other financial assets at fair value through profit or loss.

The Annual Accounts are presented in pounds Sterling and, except where otherwise indicated, have been rounded to the nearest one hundred thousand.

Going concern

The Directors have prepared forecasts for the Group, including its capital position, for a period in excess of 12 months from the date of approval of these financial statements. The Directors have also considered the effect upon the Group's business, financial position, liquidity and capital of more pessimistic, but plausible, trends in its business using stress testing and scenario analysis techniques. The resultant forecasts and projections show that the Group will be able to operate at adequate levels of both liquidity and capital for the foreseeable future. This assessment includes evaluation of the sensitivity of not classifying profit participating deferred shares (PPDS) as Common Equity Tier 1 (CET1) capital, as discussed further on pages 19 to 20 on the Strategic Report.

The Directors, therefore, consider that the Society and Group have adequate resources to continue in operational existence for the foreseeable future. Accordingly they continue to adopt the going concern basis in preparing the financial statements. For further details see page 32 of the Directors' Report.

Accounting developments

The following new or amended accounting standards and interpretations, which are relevant to the Group, have been adopted during 2016/17 but have not had a material impact on the Annual Accounts:

- Amendments to IFRS 10 'Consolidated Financial Statements', IFRS 12 'Disclosure of Interests in Other Entities' and IAS 28 'Investments in Associates and Joint Ventures'
  These amendments address issues that have arisen in the context of applying the consolidation exception for investment entities.
- Amendments to IFRS 11 'Joint Arrangements'
  This amendment requires an entity acquiring an interest in a joint operation, in which the activity of the joint operation constitutes a business, to apply the principles defined in IFRS 3 'Business Combinations'.
- Amendments to IAS 1 'Presentation of Financial Statements'
  These amendments clarify the materiality requirements in IAS 1, flexibility as to the order of the notes to the financial statements and accounting policies, criteria on presentation of subtotals in the primary financial statements and to disaggregate line items in the primary financial statements if this provides helpful information to users.
- Amendments to IAS 16 'Property, Plant and Equipment' and IAS 38 'Intangible Assets'
  These amendments clarify that the use of revenue-based methods to calculate the depreciation of an asset is inappropriate.
- Amendments to IAS 27 'Separate Financial Statements'
  These amendments allow an entity to use the equity method as described in IAS 28 to account for investments in subsidiaries, joint ventures and associates in their separate financial statements.
- Annual improvements to IFRSs 2012-2014 Cycle
  The improvements include amendments to IFRS 5 'Non-current Assets Held for Sale and Discontinued Operations', IFRS 7 'Financial Instruments: Disclosures', IAS 19 'Employee Benefits' and IAS 34 'Interim Financial Reporting'.

The following new or amended accounting standards and interpretations have been issued but are not effective for the twelve months ended 31 March 2017. The Group are monitoring developments and considering the associated impact:

- Amendments to IAS 7 'Statement of Cash Flows'
  These amendments require an entity to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including both changes arising from cash flows and non-cash changes.
- Amendments to IAS 12 'Income Taxes'
  These amendments clarify how to account for deferred tax assets for unrealised losses related to debt instruments measured at fair value.
- Amendments to IAS 40 'Investment Property'
  The amendments to IAS 40 Investment Property clarify the requirements on transfers to, or from, investment property.
- Annual improvements to IFRSs 2014-2016 Cycle
  The improvements include amendments to IFRS 1 'First-time Adoption of International Financial Reporting Standards', IAS 28 'Investments in Associates and Joint Ventures' and IFRS 12 'Disclosure of Interests in Other Entities'.
- IFRS 9 'Financial Instruments'
  IFRS 9 'Financial Instruments' replaces IAS 39 'Financial Instruments: Recognition and Measurement' and is effective for financial periods beginning on or after 1 January 2018. The standard introduces new rules for classification and measurement, impairment and hedge accounting for financial instruments. The changes to loan loss provisioning are substantial and IFRS 9 will therefore have a significant impact on the industry, requiring fundamental changes to systems and processes.

1. Accounting policies (continued)

Classification and measurement
Under IFRS 9, financial assets are classified as amortised cost or fair value (through other comprehensive income or through profit or loss), based on the business model under which they are held and the characteristics of their contractual cash flows. Initial analysis of the Group and Society balance sheets indicates that the classification elements of IFRS 9 will not have a material impact on the financial statements.

Impairment of financial assets
IFRS 9 replaces the incurred loss model prescribed by IAS 39 with a forward-looking expected loss methodology. The impairment requirements apply to all financial assets held at amortised cost or fair value through other comprehensive income, as well as certain loan commitments.

IFRS 9 introduces the concept of 'staging'. On initial recognition, a financial asset is categorised as 'stage 1' and has a 12 month expected loss provision requirement. If, at the reporting date, there has been a significant increase in credit risk since initial recognition, the asset is categorised as 'stage 2' with a defaulted account being termed 'stage 3'. IFRS 9 dictates the recognition of a lifetime expected loss allowance for assets in stage 2 or stage 3. This earlier recognition of losses is potentially material to the Group but the transitional impact cannot be reliably estimated until models have been fully developed, tested and applied to the relevant asset portfolios.

Determining whether a significant increase in credit risk has occurred is a critical aspect of the IFRS 9 methodology and one which involves judgement, based on a combination of quantitative and qualitative measures. IFRS 9 expects the calculation of expected credit losses to be unbiased and incorporate multiple, probability-weighted outcomes taking into account all reasonable and supportable information, including forecasts of future economic conditions.

The Society's IFRS 9 project is well underway, with the development of a high quality modelled residential impairment solution being carried out in partnership with external credit risk modelling specialists. The models have been designed to address the complex IFRS 9 requirements and also to align capital and accounting approaches to the estimation of credit losses as closely as possible.

Hedge accounting
Under IFRS 9, hedge accounting is more closely linked to risk management. However, macro hedging has been carved out as a separate IASB project which has not yet concluded. The Group currently intends to make the accounting policy choice, permitted by IFRS 9, to continue applying IAS 39 for all hedge relationships until such time as the new macro hedging rules are finalised.

- IFRS 15 'Revenue from Contracts with Customers'
  This standard will be effective for reporting periods beginning on or after 1 January 2018. This standard specifies how and when an entity should recognise revenue, providing a simple, principles based five-step model to be applied to all contracts with customers. The standard also prescribes further disclosure requirements in this area.
- IFRS 16 'Leases'
  The IASB announced that the new standard will come into effect for accounting periods beginning on or after 1 January 2019. IFRS 16 will replace the existing requirements in IAS 17 'Leases'. This standard provides a single lessee accounting model requiring lessees to recognise a right-of-use asset, representing its right to use the underlying asset, and a lease liability, representing its obligation to make lease payments. Exemptions are available for short term leases and leases of low value assets. IFRS 16 is subject to EU endorsement, the timing of which is uncertain.

Basis of consolidation
The Group financial statements consolidate the financial statements of the Society and its subsidiary undertakings.

Subsidiaries
Subsidiaries are all entities controlled by the Society. Control is achieved where the Group has the power to govern the financial and operating policies of an entity, has the exposure or rights to the variable returns from the involvement with the entity, and is able to use its power to affect the amount of returns for the Group. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of the subsidiaries are included in the results from the date that control commences until the date that control ceases.

The purchase method of accounting has been adopted, under which the results of subsidiary undertakings acquired or disposed of in a year are included in the Income Statement from the date of acquisition or up to the date of disposal. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the Income Statement.

Inter-company transactions, balances and unrealised gains on transactions between Group companies are eliminated. Unrealised losses are also eliminated unless the transaction provides evidence of impairment of the asset transferred. Accounting policies of subsidiaries have been changed where necessary to ensure consistency with the policies adopted by the Group.

In the Society, investments in subsidiary undertakings are carried at cost less any provisions for impairment.

Securitisation transactions
The Group has entered into securitisation transactions in which it sells mortgages to structured entities. In accordance with IAS 39, the Group continues to recognise securitised assets as loans and advances to customers. In subsequent periods, income from the securitised mortgages is recognised by the Group as disclosed below.

The equity of the structured entities created for these securitisations is not owned by the Group. However, to comply with the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004 and IFRS 10, the structured entities are included as subsidiaries in the consolidated financial statements.

The Society has entered into securitisation transactions in which it sold residential mortgages to structured entities. In accordance with IAS 39, the Society continues to recognise the securitised assets as loans and advances to customers and consequently also shows a deemed loan liability to the structured entities. The deemed loans are included within amounts due to other customers.

Segmental reporting
IFRS 8 'Operating Segments', requires operating segments to be identified on the basis of internal reports and components of the Group regularly reviewed by the chief operating decision maker to allocate resources to segments and to assess their performance. In terms of the Group, the chief operating decision maker has been deemed to be the Board of Directors.

Each segment is determined according to the distinguishable operating component of the Group that is regularly reviewed by the Group's chief operating decision maker and for which discrete financial information is available.

Information regarding the results of each reportable segment is included in note 37.

Interest receivable and expense

Interest receivable and expense are recognised in the Income Statement for all instruments measured at amortised cost or available for sale using the effective interest method.

Effective interest rate

The effective interest method is used to calculate the amortised cost of financial instruments and to recognise interest receivable or payable over the relevant period. The effective interest rate (EIR) is the rate that exactly discounts estimated cash flows (excluding credit losses) to zero, through the expected life of the instrument. The main impact for the Group relates to mortgage advances where fees, such as application and arrangement fees, and costs are incorporated in the calculation. This has the effect of spreading these fees and costs over the expected life of the mortgage. Expected lives are estimated using historic data and management judgement and the calculation is adjusted when actual experience differs from estimates, with changes in deferred amounts being recognised immediately in the Income Statement.

Fees and commissions receivable and payable

Fees and commissions are generally recognised on an accruals basis when the service has been provided. Mortgage arrangement fees and other direct costs are deferred and recognised as an adjustment to the effective interest rate on the loan. Commissions and fees arising from negotiating or participating in the negotiation of a transaction with a third party are recognised on completion of the underlying transaction.

Investment properties

Investment properties are properties held for long-term rental yields and capital appreciation. Investment properties are carried in the Statement of Financial Position at fair value, representing open market value determined annually by a qualified internal valuer and at least every five years by an external valuer. Changes in fair values are recorded in the Income Statement in accordance with IAS 40 (revised 2003). Leasehold properties held for long-term rental yields are classified as investment properties and carried at fair value.

Financial instruments

In accordance with IAS 39, all financial assets and liabilities – which include derivative financial instruments – have to be recognised in the Statement of Financial Position and measured in accordance with their assigned category.

a) Financial assets

The Group allocates financial assets to the following IAS 39 categories: financial assets at fair value through profit or loss; loans and receivables; held to maturity investments; and available for sale financial assets. Management determines the classification of its financial instruments at initial recognition. Purchases and sales of non-derivative financial assets are accounted for at settlement date.

Financial assets at fair value through profit or loss

This category comprises two sub-categories: financial assets classified as held for trading, and financial assets designated by the Group as at fair value through profit or loss upon initial recognition.

The Group uses derivative financial instruments to hedge its exposure to interest rate risk arising from operational, financing and investment activities.

In accordance with its Treasury Policy and the Building Societies Act 1986, the Group does not hold or issue derivative financial instruments for trading purposes.

Derivative financial instruments (both assets and liabilities) are initially recognised and subsequently held at fair value in the Statement of Financial Position with changes in their fair value going through the Income Statement. However, by applying the hedge accounting rules set out in IAS 39, the changes in fair value of derivatives used to hedge particular risks can either be offset in the Income Statement or deferred to equity.

There are two types of hedge accounting strategies that the Group undertakes and these are summarised below:

- hedges of the fair value of recognised assets or liabilities or unrecognised firm commitments (fair value hedges); or
- hedges of highly probable future cash flows attributable to a recognised asset or liability, or a forecasted transaction (cash flow hedges).

Hedge accounting is used for derivatives designated in this way provided that certain criteria are met.

The Group documents, at the inception of any hedging transaction, the relationship between the hedging instrument and the hedged items, as well as its risk management objective and strategy for undertaking various hedge transactions. The Group also documents its assessment, both at hedge inception and on an ongoing basis, of whether the derivatives that are used in hedging transactions are highly effective in offsetting changes in fair values or cash flows of hedged items.

i) Fair value hedges – Changes in the fair value of derivatives that are designated and qualify as fair value hedges are recorded in the Income Statement, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. If the hedge no longer meets the criteria for hedge accounting, the adjustment to the carrying amount of a hedged item, for which the effective interest method is used, is amortised to profit or loss over the remaining expected life of the previously hedged item.

ii) Cash flow hedges – The effective portion of changes in the fair value of derivatives that are designated and qualify as cash flow hedges is recognised within the Statement of Comprehensive Income and the cash flow hedging reserve. The gain or loss relating to the ineffective portion is recognised immediately in the Income Statement. Amounts accumulated in equity are recycled to the Income Statement in the periods in which the hedged item will affect profit or loss. When a hedging instrument expires or is sold, or when a hedge no longer meets the criteria for hedge accounting, any cumulative gain or loss existing in equity at that time remains in equity and is recognised when the future cash flow or forecast transaction is ultimately recognised within the Income Statement. If a forecast transaction is no longer expected to occur, the cumulative gain or loss that was reported in equity is immediately transferred to the Income Statement.

1. Accounting policies (continued)

iii) Derivatives that do not qualify for hedge accounting – Certain derivative instruments do not qualify for hedge accounting. Changes in the fair value of any derivative instrument that does not qualify for hedge accounting are recognised immediately in the Income Statement. Certain derivatives are embedded within other non-derivative financial instruments to create a hybrid instrument. Where the economic characteristics and risks of the embedded derivatives are not closely related to the economic characteristics and risk of the host instrument and where the hybrid instrument is not measured at fair value, the embedded derivative is separated from the host instrument with changes in fair value of the embedded derivative recognised in the Income Statement. Depending on the classification of the host instrument, the host instrument is then measured in accordance with the relevant IFRS standard.

The Group designates certain financial assets upon initial recognition as at fair value through profit or loss (fair value option). This designation cannot subsequently be changed. According to IAS 39, the fair value option is only applied when the following conditions are met:

- the application of the fair value option reduces or eliminates an accounting mismatch that would otherwise arise; or
- the financial asset is part of a portfolio of financial instruments which is risk managed and reported to senior management on a fair value basis; or
- the financial asset consists of a debt host and embedded derivative that must be separated.

To reduce accounting mismatch, the fair value option is applied to certain loans and receivables that are hedged with credit derivatives or interest rate swaps but for which the hedge accounting conditions of IAS 39 are not fulfilled. The loans would have been otherwise accounted for at amortised cost, whereas the derivatives are measured at fair value through profit or loss.

Financial assets for which the fair value option is applied are recognised in the notes to the accounts as financial assets designated at fair value. Fair value changes relating to financial assets designated at fair value through profit or loss are recognised as net gains on financial instruments designated at fair value through profit or loss.

Available for sale (AFS)
Available for sale investments are financial assets that are intended to be held for an indefinite period of time, which may be sold in response to needs for liquidity or changes in interest rates, exchange rates or equity prices or that are not classified as loans and receivables, held to maturity investments or financial assets at fair value through profit or loss. The Group's investment securities (e.g. certificates of deposit, gilts, etc.) are classified as available for sale assets.

Available for sale financial assets are initially recognised at fair value, which is the cash consideration including any directly attributable transaction costs, and measured subsequently at fair value with gains and losses being recognised in the consolidated Statement of Comprehensive Income, except for impairment losses and foreign exchange gains and losses, until the financial asset is derecognised, whereupon the cumulative gains and losses previously recognised in other comprehensive income are reclassified to the Income Statement as a reclassification adjustment.

Interest is calculated using the effective interest method, and foreign currency gains and losses on monetary assets classified as available for sale are recognised in the consolidated Income Statement. Dividends on available for sale equity instruments are recognised in the Income Statement in dividend income when the Group's right to receive payment is established.

The fair values of available for sale assets are based on quoted prices or, if these are not available, valuation techniques developed by the Group. These include, but are not limited to, the use of discounted cash flow models, option pricing models and recent arm's length transactions.

Loans and receivables
Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market, other than:

- those that the Group intends to sell immediately or in the short term, which are classified as held for trading, and those that the entity upon initial recognition designates as at fair value through profit or loss; or
- those that the Group upon initial recognition designates as available for sale; or
- those for which the holder may not recover substantially all of its initial investment, other than because of credit deterioration.

Loans and receivables are initially recognised at fair value – which is the cash consideration to originate or purchase the loan including any directly attributable transaction costs – and measured subsequently at amortised cost using the effective interest method. Loans and receivables are reported in the Statement of Financial Position as loans and advances to credit institutions or customers or as investment securities. Interest on loans is included in the consolidated Income Statement and is reported as interest receivable and similar income. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the loan and recognised in the Income Statement as impairment on loans and advances.

Held to maturity financial assets
Held to maturity investments are non-derivative financial assets with fixed or determinable payments and fixed maturities that the Group's management has the positive intention and ability to hold to maturity, other than:

- those that the Group upon initial recognition designates as at fair value through profit or loss;
- those that the Group designates as available for sale; and
- those that meet the definition of loans and receivables.

These are initially recognised at fair value including direct and incremental transaction costs and measured subsequently at amortised cost, using the effective interest method. Interest on held to maturity investments is included in the Income Statement and reported as interest receivable and similar income. In the case of an impairment, the impairment loss is reported as a deduction from the carrying value of the investment and recognised in the Income Statement.

b) Financial liabilities
The Group's holding in financial liabilities is in financial liabilities at fair value through profit or loss, financial liabilities at amortised cost and hedging derivatives. Financial liabilities are derecognised when extinguished.

All financial liabilities including shares, deposits, debt securities in issue and subordinated liabilities held by the Group are recognised initially at fair value, being the issue proceeds, net of premia, discounts and directly attributable transaction costs incurred.

Financial liabilities are subsequently measured at amortised cost using the effective interest method, except for those financial liabilities, for example derivative liabilities, which are measured at fair value through profit or loss.

c) Financial instruments designated at fair value through profit or loss

Financial instruments, other than those held for trading, are classified in this category if they meet one or more of the criteria set out below, and are so designated by management. The Group may designate financial instruments at fair value when the designation eliminates or significantly reduces measurement or recognition inconsistencies that would otherwise arise from measuring financial assets or financial liabilities, or recognising gains and losses on them, on different bases. Under this criteria, the main classes of financial instruments designated by the Group are where:

- the assets or liabilities are managed, evaluated and reported internally on a fair value basis; or
- the asset or liability contains an embedded derivative that significantly modifies the cash flows that would otherwise be required under the contract.

The fair value designation, once made, is irrevocable. Designation of financial assets and financial liabilities are recognised when the Group enters into the contractual provisions of the arrangements with counterparties and are normally derecognised when sold (assets) or extinguished (liabilities). Measurement is initially at fair value, with transaction costs taken directly to the Income Statement. Subsequently, the fair values are remeasured, and gains and losses from changes therein are recognised in net income from financial instruments designated at fair value. Note 31 sets out the amount of each class of financial asset or liability that has been designated at fair value through profit or loss.

d) Impairment of financial assets

Impairment of mortgage loans and advances

The Group assesses at each year end date whether there is objective evidence that a financial asset is impaired. Objective evidence of impairment can be defined as one or more events occurring after the initial recognition of the asset that have an impact on the estimated future cash flows of the financial asset that can be reliably estimated.

The Group first assesses whether objective evidence of impairment exists for financial assets using the following criteria:

- Deterioration in payment status;
- Tenant failure;
- Expected future increase in arrears due to change in loan status;
- Breach of loan covenants; and
- Any other information suggesting that a loss is likely in the short to medium term.

If the Group determines that no objective evidence of impairment exists for an individually assessed financial asset, whether significant or not, it includes the asset in a group of financial assets with similar credit risk characteristics and collectively assesses them for impairment. Assets that are individually assessed for impairment, and for which an impairment loss is or continues to be recognised, are not included in a collective assessment of impairment.

A collective provision is made against a group of loans and advances where there is objective evidence that credit losses have been incurred but not identified at the reporting date. The collective impairment calculation takes into account a number of factors, including forbearance measures applied to the loans, such as term extensions and short-term interest only conversions.

If there is objective evidence of an impairment of loans and receivables, the amount of the loss is measured as the difference between the asset's carrying amount and the present value of estimated future cash flows (excluding future credit losses that have not been incurred) discounted at the financial asset's original effective interest rate. This calculation takes into account the Group's experience of default rates, loss emergence periods, the effect of regional movements in house prices based upon a recognised index and adjustments to allow for ultimate forced sales values and realisation costs. The amount of the loss is recognised in the Income Statement.

Where a loan is not recoverable, it is written off against the related provision for loan impairment once all the necessary procedures have been completed and the amount of the loss has been determined. Subsequent recoveries of amounts previously written off decrease the amount of impairment losses recorded in the Income Statement.

Impairment losses on investment securities

At each year end date the Group assesses whether or not there is objective evidence that individual investment securities are impaired. In determining whether there is any objective evidence of impairment the Group takes into account a number of factors including:

- significant financial difficulties of the issuer or obligor;
- any breach of contract or covenants;
- the granting of any concession or rearrangement of terms;
- the disappearance of an active market;
- any significant downgrade of ratings; and
- any significant reduction in market value.

In some cases a significant adverse change in one of the above factors will cause the Group to determine that there is objective evidence of impairment. In other cases it may not be possible to identify a single event that identifies impairment. The Group may additionally determine that there is impairment where there are a number of factors contributing to that view.

Where the Group determines that there is objective evidence of impairment or that trigger events exist, then, in the case of available for sale instruments, the cumulative gain or loss that had been recognised directly in reserves is removed from reserves and recognised in the Income Statement. In the case of held to maturity instruments an appropriate charge is made to the Income Statement.

If, in a subsequent period, the fair value of an investment security classified as available for sale increases and the increase can be related to an event occurring after the impairment loss was recognised through the Income Statement, the impairment loss shall be reversed, with the amount of the reversal recognised through the Income Statement.

Impairment losses on investments in subsidiary undertakings

The Society assesses, at each reporting date, whether there is any indication that its investments in subsidiary companies are impaired. If any indication of impairment exists, the Society compares the relevant asset's recoverable amount with its carrying value and, if an impairment loss has arisen, recognises it in the Income Statement immediately.

1. Accounting policies (continued)

The recoverable amount of the investment is calculated with reference to the present value of the subsidiary's estimated future cash flows, primarily those arising from the continued trading of the subsidiary. This approach is based on the assumption that the Society, by virtue of control, is able to extract the subsidiary's cash flows in the form of loan repayment and/or dividends. In line with IAS 39, the discount rate used to arrive at the present value of future cash flows is the intergroup interest charge rate representing the EIR of the investment asset being assessed.

e) Derecognition of financial assets and liabilities

The Group's policy is to derecognise financial assets when the contractual right to the cash flows from the financial asset expires. The Group also derecognises financial assets that it transfers to another party provided the transfer of the asset also transfers the right to receive the cash flows of the financial asset and substantially all the risks and rewards of ownership.

The Group derecognises financial liabilities only when the obligation specified in the contract is discharged, cancelled or has expired.

f) Determination of fair value

The Group determines fair values by the three tier valuation hierarchy as defined within IFRS 13 'Fair Value Measurement' and Amendments to IFRS 7 'Financial Instruments: Disclosures'.

Level 1: For financial instruments traded in active markets, the determination of fair values of financial assets and financial liabilities is based on quoted market prices or dealer price quotations. This includes listed equity securities and quoted debt instruments on major exchanges (for example, FTSE, NYSE) and broker quotes from Bloomberg and Reuters.

A financial instrument is regarded as quoted in an active market if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and those prices represent actual and regularly occurring market transactions on an arm's length basis. If the above criteria are not met, the market is regarded as being inactive. Indications that a market is inactive are when there is a wide bid-offer spread or significant increase in the bid-offer spread or there are few recent transactions.

Level 2: For all other financial instruments, fair value is determined using valuation techniques. In these techniques, fair values are estimated from observable data in respect of similar financial instruments, using models to estimate the present value of expected future cash flows or other valuation techniques, using inputs (for example, LIBOR yield curve, FX rates, volatilities and counterparty spreads) existing at the reporting dates.

The Group uses widely recognised valuation models for determining fair values of non-standardised financial instruments of lower complexity, such as options or interest rate and currency swaps. For these financial instruments, inputs into models are generally market observable.

Level 3: Fair value is determined using valuation techniques where significant inputs are not based on observable market data.

The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length.

g) Sale and repurchase agreements

Investment and other securities may be lent or sold subject to a commitment to repurchase them. Where substantially all of the risks and rewards of ownership remain with the Group, the securities are retained on the Statement of Financial Position. The counterparty liability is recognised separately in the Statement of Financial Position as appropriate. The difference between the sale and repurchase price is accrued over the life of the agreements.

Intangible assets

Goodwill

Goodwill arising on the acquisition of subsidiary undertakings, joint ventures, associates or businesses represents the excess of the fair value of consideration over the fair value of identifiable net assets and contingent liabilities acquired at the date of acquisition. In accordance with IFRS 3, 'Business Combinations', goodwill is not systematically amortised but is initially recognised as an asset at cost and is subsequently measured at cost less any accumulated impairment losses. Goodwill which is recognised as an asset is reviewed for impairment at least annually. Any impairment is recognised in the Income Statement and is not subsequently reversed.

For the purpose of impairment testing, goodwill is allocated to each of the Group's applicable cash generating units. Each unit is tested at least annually and reviewed for impairment indicators at each reporting date, with a further impairment test performed if indicators deem necessary. The impairment test compares the carrying value of goodwill to the higher of its fair value less costs of sale and its value in use. The value in use calculations are carried out by discounting the future cash flows of the cash generating unit.

On the sale of a subsidiary undertaking, the profit or loss on sale is calculated after charging or crediting the net book value of any related goodwill. Negative goodwill arising on an acquisition would be recognised directly in the Income Statement.

Computer software

Computer software which is not an integral part of the related hardware is recorded as an intangible asset. The identifiable and directly associated external and internal costs of acquiring and developing software are capitalised where the software is controlled by the Group, and where it is probable that future economic benefits that exceed its cost will flow from its use over more than one year. Intangible assets are held at amortised cost, amortisation is charged to the Income Statement on a straight line basis over the estimated useful life of 3 to 7 years; they are subject to regular impairment reviews. Costs associated with maintaining software are recognised as an expense when incurred.

Property, plant and equipment

Land and buildings comprise mainly branches and offices. All property, except specialised administration buildings, is stated at valuation less depreciation. Specialised administration buildings and plant and equipment are stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. All gains on the revaluation of property are recognised in the revaluation reserve when they arise.

Subsequent costs are included in the asset's carrying amount or are recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Group and the cost of the item can be measured reliably. All other repairs and maintenance are charged to the Income Statement during the financial period in which they are incurred.

Land is not depreciated. Depreciation on other assets is calculated using the straight line method (unless otherwise stated) to allocate their cost less their residual values over their estimated useful lives, as follows:

Freehold branches and non-specialised buildings	Up to 50 years
Specialised administration buildings	Up to 25 years
Short leasehold properties	Annual instalments over the period of the lease
Equipment, fixtures and fittings and motor vehicles	
• Office equipment	3 to 7 years
• Computer equipment	3 to 7 years
• Motor vehicles	25% per annum reducing balance
• Refurbishments	5 to 10 years

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each year end date. Assets that are subject to amortisation are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount. The recoverable amount is the higher of the asset's fair value less costs to sell and value in use.

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the Income Statement.

Leases
The leases entered into by the Group are primarily operating leases. The total payments made under operating leases are charged to the Income Statement on a straight line basis over the period of the lease.

When an operating lease is terminated before the lease period has expired, any payment required to be made to the lessor by way of penalty is recognised as an expense in the period in which termination takes place.

Cash and cash equivalents
For the purposes of the cash flow statement, cash comprises cash in hand and loans and advances to credit institutions repayable on demand. Cash equivalents comprise highly liquid investments that are convertible into cash with an insignificant risk of changes in value, with maturities of 90 days or less.

Taxation
Tax on the profit/loss for the year comprises current tax and deferred tax. Income tax is recognised in the Income Statement except to the extent that it relates to items recognised directly in equity, in which case it is recognised in other comprehensive income within the Statement of Comprehensive Income.

Current tax is the expected tax payable/receivable on the taxable income/expense for the year, using the tax rate which applies to the accounting period ending at the date of the Statement of Financial Position, and any adjustment to tax payable in respect of previous years.

Deferred tax is provided in full, using the balance sheet liability method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is determined using tax rates (and laws) that have been substantively enacted by the year end date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised where it is probable that future taxable profits will be available against which the temporary differences can be utilised.

Provisions and contingent liabilities
Provisions are recognised when the Group has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation and the amount can be reliably estimated.

A possible obligation that arises from past events and whose existence will be confirmed only by the occurrence or non-occurrence of one or more uncertain future events, not wholly within the control of the Group, is a contingent liability. A contingent liability is disclosed but not recognised in the Statement of Financial Position.

Employee benefits
The Group provides both a defined benefit scheme (closed to new employees from 2002/3 and accruals from 2009/10) and a defined contribution scheme on behalf of staff and Directors. The defined benefit scheme is funded by contributions from the Society at rates assessed by independent actuaries. These contributions are invested separately from the Group's assets. The Scheme assets are measured at market value at each year end date and the liabilities are measured using the projected unit valuation method, by qualified actuaries, discounted using a corporate bond rate. The resulting pension scheme surplus or deficit is recognised in the Statement of Financial Position.

Actuarial gains and losses are recognised in full in the period in which they occur. As permitted by the revised standard, actuarial gains and losses are recognised outside profit or loss and presented in other comprehensive income.

Net interest, comprising interest income on plan assets less interest costs on scheme liabilities, and other expenses relating to the defined benefit pension scheme are recognised in the Income Statement. Actuarial gains or losses, that are gains or losses arising from differences between previous actuarial assumptions and actual experience, are recognised in the Statement of Comprehensive Income.

For defined contribution plans, the contributions are recognised as employee benefit expense in the Income Statement when they are due, in accordance with the rules of the scheme. Prepaid contributions are recognised as an asset to the extent that a cash refund or a reduction in the future payments is available.

Critical accounting estimates and judgements in applying accounting policies
The Group makes estimates and assumptions that affect the reported amounts of assets and liabilities within the next financial year. Estimates and judgements are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

Pensions
The Group operates a defined benefit pension scheme. Significant judgements (on areas such as future interest and inflation rates and mortality rates) have to be exercised in estimating the value of the assets and liabilities of the scheme.

These judgements, which are based upon the Board receiving external advice from the scheme actuaries, are outlined in note 30 to the Accounts.

1. Accounting policies (continued)

Impairment losses on loans and advances
The creation of impairment provisions for a portfolio of mortgage loans is inherently uncertain and requires the exercise of a significant degree of judgement. Provisions are calculated using historic default and loss experience, but require judgement to be exercised in predicting economic conditions (e.g. interest rates and house prices), customer behaviour (e.g. default rates) and the length of time before impairments are identified (emergence period). The most critical estimate is of the level of house prices where a variance of 1% equates to £0.2m of provision. Other sensitivities include the emergence period, where a variance of six months equates to £0.4m, and the loss given default rate, where a 10% variance equates to £0.6m of provision.

For commercial mortgages the key sensitivities are interest rates, rental yields and exit yields, the rental yield impacting on annual returns and also the value of the commercial properties which provide security. A 0.5% increase in the current and projected future interest rates would increase commercial provision requirements by £7.0m before any compensating economic hedge arrangements in place, which would be expected to offset a substantial proportion of any such interest rate sensitivity. A 0.25% reduction in expected rental income would increase provision requirements by £3.5m. A 0.25% increase in expected exit yield requirements would increase provisions by £8.6m.

Impairment of treasury investments
Treasury investments are regularly reviewed for objective evidence of impairment. In determining whether objective evidence exists, the Group considers, amongst other factors, current market conditions, fair value volatility, appropriateness of valuation techniques and the financial stability of the counterparty.

Effective interest rate
The calculation of an effective interest rate requires the Group to make assumptions around the expected lives of mortgages. Management regularly reviews these assumptions and compares with actual results.

If the average lives of the mortgages were to increase by 5%, the carrying value of mortgages would change by £1.9m with a corresponding change to income.

Investment properties
The calculation of the fair value of investment properties involves house price assumptions which are regularly reviewed by management.

If house prices were to change by 5%, the carrying value of the investment properties would change by £6.4m with a corresponding change to income.

Taxation
Significant estimates are required in determining the provision for corporation tax. There are a number of transactions for which the final tax determination is uncertain at the year end date.

Fair value of derivatives and financial assets
The most reliable fair values of derivative financial instruments and available for sale assets are quoted market prices in an actively traded market. Where there is no active market, valuation techniques are used. Techniques adopted include valuation models used to calculate the present value of expected future cash flows, and options pricing models, if market values are not available. These techniques make use of observable market data and hence fair value estimates can be considered to be reliable. Where inputs are not observable they may be based on historic data. Changes in assumptions used in the models could affect the reported fair value of derivatives and available for sale assets.

Where previously active markets no longer provide prices, other market sources are monitored, such as real-time market information, custodian and independent financial institution valuations, and management judgement is exercised in determining fair values for these or similar instruments.

Basis risk derivatives are valued using discounted cash flow models, using observable market data and will be sensitive to benchmark interest rate curves.

Deferred tax assets
A deferred tax asset is recognised to the extent that it is probable that future taxable profits will be available against which deductible temporary differences can be utilised. The recognition of the deferred tax asset is dependent upon the projection of future taxable profits and future reversals of existing taxable temporary differences and it is necessary for management to evaluate whether the deferred tax asset has arisen due to temporary factors or is instead indicative of a permanent decline in earnings.

Management has made detailed forecasts of future taxable income in order to determine that profits will be available to offset the deferred tax asset. These projections are based on business plans, future capital requirements and the current economic situation. They include assumptions about the depth and severity of potential further house price depreciation and about the UK economy, including unemployment levels and their related impact on credit losses.

The assumptions surrounding future expected credit losses and increases in the Bank Rate of interest represent the most subjective areas of judgement in management's projections of future taxable profits. Management's forecasts support the assumption that it is probable that the results of future operations will generate sufficient taxable income to utilise the deferred tax assets and it is on this basis that the deferred tax assets have been recognised. Deferred tax has been recognised at rates between 17% and 19%, being the rates substantively enacted at the date of the Statement of Financial Position and expected to apply when the deferred tax assets are realised.

Securitisation transactions
In order to determine whether the Society controls a structured entity or not, the Society has to make judgements about risks and rewards and assess the ability to make operational decisions for the structured entity in question. In many instances, elements are present that, considered in isolation, indicate control or lack of control over a structured entity, but when considered together make it difficult to reach a clear conclusion. When assessing whether the Group has to consolidate a structured entity it evaluates a range of factors. The following are the prime factors that are considered and the applicable accounting treatment in each case:

- When the Group, in substance, controls the entity to which financial assets have been transferred, the entity is included in these consolidated financial statements and the transferred assets are recognised in the Group's Statement of Financial Position;
- When the Group transfers financial assets to an unconsolidated entity and it retains substantially all of the risk and rewards relating to the transferred assets, the transferred assets are recognised in the Group's Statement of Financial Position;
- When the Group transfers substantially all the risks and rewards relating to the transferred financial assets to an unconsolidated entity, the assets are derecognised from the Group's Statement of Financial Position; and
- When the Group neither transfers nor retains substantially all the risks and rewards relating to a transferred financial asset and it retains control of the transferred asset, the Group continues to recognise the transferred financial asset to the extent of its continuing involvement in that transferred financial asset. Details of the Group's securitisation activities are given in note 13.

2. Interest receivable and similar income

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
On financial assets not at fair value through profit or loss:				
Loans fully secured on residential property	**99.2**	108.4	**64.9**	61.0
Other loans				
Connected undertakings	**-**	-	**42.2**	56.7
Loans fully secured on land	**21.0**	28.6	**1.2**	1.2
Investment securities	**5.1**	5.0	**12.2**	13.5
Other liquid assets	**1.0**	1.5	**0.9**	1.2
On financial assets at fair value through profit or loss:				
Net expense on derivative financial instruments	**(18.1)**	(18.2)	**(17.6)**	(15.6)
Loans fully secured on land	**0.7**	1.4	**-**	-
Total interest income	**108.9**	126.7	**103.8**	118.0
Interest receivable includes:				
Income from fixed income securities	**2.7**	3.0	**2.7**	3.0

Included within interest receivable and similar income is interest accrued on impaired residential mortgage assets: Group £1.2m (2015/16: £1.8m) and Society £1.0m (2015/16: £1.2m) and interest accrued on impaired commercial mortgage assets: Group £4.3m (2015/16: £6.3m) and Society £nil (2015/16: £nil).

3. Interest expense and similar charges

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
On financial liabilities not at fair value through profit or loss:				
Shares held by individuals	**41.7**	51.5	**41.7**	51.5
Deposits from banks and other deposits	**6.5**	7.6	**5.7**	6.6
Interest on debt securities in issue	**5.0**	7.1	**-**	0.9
Deemed loans	**-**	-	**6.5**	9.0
On financial liabilities at fair value through profit or loss:				
Net income on derivative financial instruments	**(0.4)**	(0.6)	**(0.4)**	(0.6)
Interest on debt securities in issue	**0.8**	1.1	**-**	-
Total interest expense	**53.6**	66.7	**53.5**	67.4

4. Other operating income

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Other operating income includes:				
Rent receivable on investment property	**6.5**	6.2	**-**	-
Operating expenses on investment property	**(2.3)**	(2.1)	**-**	-
Pension fund net interest (note 30)	**-**	(0.1)	**-**	(0.1)
Dividends received from Group undertakings	**-**	-	**37.5**	30.7
Other	**(0.1)**	(0.1)	**(0.1)**	(0.1)
Total other operating income	**4.1**	3.9	**37.4**	30.5

5. Net realised profits

Net realised profits arise on the sale of treasury instruments. The Society is required to periodically sell a proportion of its liquid assets to prove that they remain liquid. By their nature these sources of income are highly variable.

6. Administrative expenses

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Staff costs				
Wages and salaries	**23.7**	22.6	**23.4**	22.4
Social security costs	**2.2**	1.8	**2.2**	1.8
Other pension costs	**1.5**	1.4	**1.5**	1.3
Rental charges payable under operating leases	**0.6**	0.5	**0.6**	0.5
Other administrative expenses	**16.4**	15.7	**12.7**	11.8
	44.4	42.0	**40.4**	37.8
Other administrative expenses include:				
Remuneration of auditor (excluding VAT element)				
Audit of these financial statements	**0.2**	0.1	**0.2**	0.1
Audit of the subsidiary financial statements	**0.1**	0.1	**-**	-
Other assurance services	**-**	0.1	**-**	0.1

Wages and salaries include £0.1m (2015/16: £0.3m) redundancy costs paid as part of the restructuring and rationalisation of the Group's cost base.

7. Employee numbers

	Group 2017	Group 2016	**Society 2017**	Society 2016
The average number of employees employed throughout the year was:				
Full time	**620**	616	**613**	609
Part time	**138**	124	**137**	123
	758	740	**750**	732
Building Society				
Central administration	**535**	490	**535**	490
Branches	**215**	242	**215**	242
Subsidiaries	**8**	8	**-**	-
	758	740	**750**	732

All employees were employed within the United Kingdom.

8. Directors' emoluments

Total Directors' emoluments including expenses amounted to £1.648m (2015/16: £1.564m). Full details are given in the Directors' Remuneration Report on pages 40 to 46.

9. Taxation

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
UK corporation tax at 20% (2015/16: 20%)	**0.9**	2.5	**0.9**	2.5
Corporation tax - adjustment in respect of prior years	**-**	(1.2)	**(0.9)**	(1.2)
Total current tax	**0.9**	1.3	**-**	1.3
Deferred tax				
Current year	**5.6**	1.8	**4.5**	0.6
Adjustment in respect of prior periods	**(0.5)**	1.0	**(1.5)**	(2.2)
Tax on (loss)/profit on ordinary activities	**6.0**	4.1	**3.0**	(0.3)

UK corporation tax has been calculated at the applicable prevailing rate.

The tax charge for the year differs to that calculated using the UK standard rate of tax, due mainly to the write down of deferred tax assets in relation to brought forward losses to a level expected to be recoverable in the next five years. The estimated recoverable amount reduced following the outcome of the legal case which affected the Group's ability to vary the interest rate applicable to certain buy to let loans.

The tax charge is reconciled to the (loss)/profit before tax in the Income Statement as follows:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
(Loss)/Profit before tax	**(19.8)**	13.5	**5.8**	7.8
(Loss)/Profit before tax multiplied by the UK standard rate of tax of 20% (2015/16: 20%)	**(4.0)**	2.7	**1.2**	1.6
Effects of:				
Income not taxable and expenses not deductible for tax purposes	**2.2**	0.7	**0.6**	0.5
Changes to tax rate	**0.1**	1.4	**0.2**	1.0
Adjustment in respect of prior years	**(0.5)**	(0.2)	**(2.4)**	(3.4)
Transfer pricing adjustments	**-**	-	**(1.7)**	-
Write down of deferred tax assets	**9.2**	-	**5.1**	-
Revaluation	**(1.0)**	(0.5)	**-**	-
Tax charge	**6.0**	4.1	**3.0**	(0.3)

10. Cash and balances with the Bank of England

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Cash in hand	**2.4**	2.2	**2.4**	2.2
Cash ratio deposit with the Bank of England	**7.2**	6.7	**7.2**	6.7
Other deposits with the Bank of England	**285.2**	206.5	**285.2**	206.5
	294.8	215.4	**294.8**	215.4

Cash ratio deposits are mandatory deposits with the Bank of England which are not available for use in the Group's day-to-day operations. Cash in hand and the mandatory deposit with the Bank of England are non-interest bearing.

11. Investment securities

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Investment securities: available for sale				
Listed	**385.0**	359.0	**385.0**	359.0
Unlisted	**-**	51.1	**-**	51.1
Investment securities: held to maturity				
Listed	**-**	-	**810.5**	889.9
Total investment securities	**385.0**	410.1	**1,195.5**	1,300.0

In accordance with IAS 39, available for sale investment securities are stated at fair value and held to maturity investment securities are stated at amortised cost. Gains/(losses) on disposal of investment securities are disclosed as net realised profits/(losses) on the face of the Income Statement.

The movement in investment securities may be summarised as follows:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
At beginning of year	**410.1**	274.3	**1,300.0**	1,270.1
Additions	**229.9**	440.0	**229.9**	440.0
Disposals (sale and redemption)	**(255.5)**	(302.0)	**(334.9)**	(407.9)
Gains/(Losses) from changes in fair value	**0.5**	(2.2)	**0.5**	(2.2)
At end of year	**385.0**	410.1	**1,195.5**	1,300.0

The Directors consider that the primary purpose for holding investment securities is prudential. The investment securities are held as liquid assets with the intention of use on a continuing basis in the Group's activities.

12. Derivative financial instruments

A description of the derivative financial instruments used by the Group for hedging purposes is given in note 33.

The fair values of derivative instruments held at 31 March 2017 are set out below. The other derivatives held for hedging are held for economic hedging purposes.

	Notional principal amount 2017 £m	**Fair values**	
Group		**Assets 2017 £m**	**Liabilities 2017 £m**
Derivatives held for hedging			
Derivatives designated as fair value hedges	**1,436.5**	**2.9**	**(53.7)**
Derivatives designated as cash flow hedges	**112.0**	**-**	**(0.3)**
Other derivatives held for hedging	**698.5**	**3.4**	**(15.0)**
Total derivative assets/(liabilities) held for hedging	**2,247.0**	**6.3**	**(69.0)**

Group	Notional principal amount 2016 £m	Fair values Assets 2016 £m	Liabilities 2016 £m
Derivatives held for hedging			
Derivatives designated as fair value hedges	1,323.7	2.1	(62.9)
Derivatives designated as cash flow hedges	133.0	0.1	-
Other derivatives held for hedging	756.0	6.7	(14.2)
Total derivative assets/(liabilities) held for hedging	2,212.7	8.9	(77.1)

Society	**Notional principal amount 2017 £m**	**Fair values Assets 2017 £m**	**Liabilities 2017 £m**
Derivatives held for hedging			
Derivatives designated as fair value hedges	**1,417.2**	**2.8**	**(48.5)**
Other derivatives held for hedging	**659.1**	**3.4**	**(11.2)**
Total derivative assets/(liabilities) held for hedging	**2,076.3**	**6.2**	**(59.7)**

Society	Notional principal amount 2016 £m	Fair values Assets 2016 £m	Liabilities 2016 £m
Derivatives held for hedging			
Derivatives designated as fair value hedges	1,437.1	2.1	(57.3)
Other derivatives held for hedging	548.0	6.7	(10.1)
Total derivative assets/(liabilities) held for hedging	1,985.1	8.8	(67.4)

13. Loans and advances to customers

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Loans and receivables				
Loans fully secured on residential property	**4,253.8**	4,131.2	**2,642.5**	2,357.3
Other loans				
Loans fully secured on land	**506.7**	584.4	**13.8**	13.8
Other loans	**-**	0.1	**-**	-
	4,760.5	4,715.7	**2,656.3**	2,371.1
At fair value through profit or loss				
Other loans				
Loans fully secured on land	**17.8**	26.0	**-**	-
	4,778.3	4,741.7	**2,656.3**	2,371.1
Fair value adjustment for hedged risk	**53.9**	62.0	**16.2**	19.6
Less: impairment provisions	**(55.7)**	(64.7)	**(8.8)**	(10.6)
	4,776.5	4,739.0	**2,663.7**	2,380.1

13. Loans and advances to customers (continued)

Included within loans and advances to customers are £587.5m (2015/16: £679.6m) of commercial lending balances of which £73.4m (2015/16: £92.1m) have been sold by the Group to bankruptcy remote structured entities. A further £1,012.6m (2015/16: £1,165.8m) of residential mortgage balances, included with loans and advances, have also been sold by the Group to structured entities. The structured entities have been funded by issuing mortgage backed securities (MBSs) of which £810.5m (2015/16: £889.9m) are held by the Group.

The Group has made subordinated loans to the structured entities to provide some level of credit enhancement to the MBSs. In future periods the Group will earn interest income on the subordinated loans and fees for managing the loans. The Group will earn deferred consideration once the cash flows generated by the structured entities have been used to pay interest and capital to the holders of the MBSs. Since the Group maintains substantially all of the risks (key risk being an exposure to credit risk through the subordinated loan agreements) and rewards emanating from the mortgages, they have been retained on the Group's Statement of Financial Position in accordance with IAS 39.

14. Allowance for losses on loans and advances

	Loans fully secured on residential property		**Loans fully secured on land**		**Total**		
Group	**Individual £m**	**Collective £m**	**Individual £m**	**Collective £m**	**Individual £m**	**Collective £m**	**Total £m**
At 1 April 2016	11.8	9.0	34.8	9.1	46.6	18.1	**64.7**
Amounts written off	(1.0)	-	(15.3)	-	(16.3)	-	**(16.3)**
(Credit)/Charge for the year comprising:							
Provision for loan impairment	(0.7)	(0.8)	6.0	4.8	5.3	4.0	**9.3**
Change in carrying value of debt securities in issue	-	-	0.3	-	0.3	-	**0.3**
Adjustments to provisions resulting from recoveries	(2.0)	-	-	-	(2.0)	-	**(2.0)**
(Credit)/Charge for the year	(2.7)	(0.8)	6.3	4.8	3.6	4.0	**7.6**
Non-recourse finance on securitised advances	-	-	(0.3)	-	(0.3)	-	**(0.3)**
At 31 March 2017	**8.1**	**8.2**	**25.5**	**13.9**	**33.6**	**22.1**	**55.7**

	Loans fully secured on residential property		Loans fully secured on land		Total		
Group	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
At 1 April 2015	15.8	8.7	37.3	7.9	53.1	16.6	69.7
Amounts written off	(3.8)	-	(9.4)	-	(13.2)	-	(13.2)
Charge/(Credit) for the year comprising:							
Provision for loan impairment	0.8	0.3	8.0	1.2	8.8	1.5	10.3
Change in carrying value of debt securities in issue	-	-	(0.5)	0.4	(0.5)	0.4	(0.1)
Adjustments to provisions resulting from recoveries	(1.0)	-	(1.1)	-	(2.1)	-	(2.1)
(Credit)/Charge for the year	(0.2)	0.3	6.4	1.6	6.2	1.9	8.1
Non-recourse finance on securitised advances	-	-	0.5	(0.4)	0.5	(0.4)	0.1
At 31 March 2016	11.8	9.0	34.8	9.1	46.6	18.1	64.7

Included within loans fully secured on residential property are loans originated through the commercial division. At 31 March 2017, the provision against these loans totalled £nil (2015/16: £nil), with a net credit for the year of £nil (2015/16: £0.1m). The total provision balance relating to the commercial division is £39.4m (2015/16: £43.9m), with a charge for the year of £11.1m (2015/16: £7.9m).

During the year there were impairment credits of £0.3m (2015/16: charges of £0.1m) against loans in structured entities, Sandwell Commercial Finance No.1 Plc: £0.2m credit (2015/16: £0.6m charge) and Sandwell Commercial Finance No. 2 Plc: £0.1m credit (2015/16: £0.5m credit). The gains or losses from these impairments are borne by the external loan note holders as they exceed the first loss exposure held by the Group. Impairment provisions at the end of the year include £1.8m (2015/16: £4.2m) against loans in structured entities, Sandwell Commercial Finance No.1 Plc: £nil (2015/16: £2.4m) and Sandwell Commercial Finance No. 2 Plc: £1.8m (2015/16: £1.8m). The carrying value of the external loan notes has been adjusted by an equivalent amount.

Society	Loans fully secured on residential property		Loans fully secured on land		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
At 1 April 2016	7.1	3.5	-	-	7.1	3.5	**10.6**
Amounts written off	(0.6)	-	-	-	(0.6)	-	**(0.6)**
Credit for the year comprising:							
Release of provision for loan impairment	-	(0.4)	-	-	-	(0.4)	**(0.4)**
Adjustments to provisions resulting from recoveries	(0.8)	-	-	-	(0.8)	-	**(0.8)**
Credit for the year	(0.8)	(0.4)	-	-	(0.8)	(0.4)	**(1.2)**
At 31 March 2017	**5.7**	**3.1**	**-**	**-**	**5.7**	**3.1**	**8.8**

Society	Loans fully secured on residential property		Loans fully secured on land		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
At 1 April 2015	8.7	4.3	-	-	8.7	4.3	13.0
Amounts written off	(0.8)	-	-	-	(0.8)	-	(0.8)
Credit for the year comprising:							
Release of provision for loan impairment	(0.4)	(0.8)	-	-	(0.4)	(0.8)	(1.2)
Adjustments to provisions resulting from recoveries	(0.4)	-	-	-	(0.4)	-	(0.4)
Credit for the year	(0.8)	(0.8)	-	-	(0.8)	(0.8)	(1.6)
At 31 March 2016	7.1	3.5	-	-	7.1	3.5	10.6

15. Investments

Society	Shares in subsidiary undertakings		Loans to subsidiary undertakings		Total	
	2017 £m	2016 £m	**2017 £m**	2016 £m	**2017 £m**	2016 £m
Cost						
At beginning of year	**0.6**	0.6	**1,709.3**	1,910.7	**1,709.9**	1,911.3
Decrease for the year	**-**	-	**(104.8)**	(201.4)	**(104.8)**	(201.4)
At end of year	**0.6**	0.6	**1,604.5**	1,709.3	**1,605.1**	1,709.9
Provisions						
At beginning of year	**-**	-	**40.7**	9.9	**40.7**	9.9
Charge for the year	**-**	-	**37.5**	30.8	**37.5**	30.8
At end of year	**-**	-	**78.2**	40.7	**78.2**	40.7
Net book value at end of year	**0.6**	0.6	**1,526.3**	1,668.6	**1,526.9**	1,669.2

Investments in subsidiary undertakings are financial fixed assets and are held at cost less impairment. All subsidiary loans are provided at open market rates.

Following continued contraction of the commercial mortgage book and additional losses within West Bromwich Commercial Limited, the Society has carried out a further review of the carrying value of its investment in West Bromwich Commercial Limited. The value of the Society's investment in West Bromwich Commercial Limited has been calculated by estimating the future cash flows that are expected to arise from the underlying net assets of the subsidiary. The cash flows predominantly consist of those arising from the continued trading of the subsidiary (e.g. interest from loans secured on commercial real estate). In line with IAS 39, the appropriate discount rate used is that applicable to the intra-group loan account. Following this review it has been necessary to write down the value of the investment by £37.5m (2015/16: £30.8m).

15. Investments (continued)

The Society holds directly (unless otherwise stated) the following interests in key subsidiary undertakings, all of which are registered in England:

Name	Major activities	Class of shares held	Interest of Society
West Bromwich Mortgage Company Limited	Residential mortgage lending	Ordinary £1 shares	100%
West Bromwich Commercial Limited	Commercial mortgage lending	Ordinary £1 shares	100%
CL Mortgages Limited (1)	Residential mortgage lending	Ordinary £1 shares	100%
West Bromwich Homes Limited	Investment in property for rental	Ordinary £1 shares	100%
Insignia Finance Limited	Second charge lending	Ordinary £500 shares	100%
White Label Lending Limited (2)	Second charge lending	Ordinary £1 shares	100%

(1) The entire share capital of CL Mortgages Limited is held by West Bromwich Mortgage Company Limited.

(2) The entire share capital of White Label Lending Limited is held by Insignia Finance Limited.

Securitisation entities
The results of the following securitisation entities are consolidated into the results of the Group under the rules and guidance of IFRS 10:

Name	Country of incorporation	Principal activity
Sandwell Finance Holdings Limited	United Kingdom	Holding company
Sandwell Commercial Finance No. 1 Plc	United Kingdom	Securitisation entity
Sandwell Commercial Finance No. 2 Plc	United Kingdom	Securitisation entity
Hawthorn Hold Co Limited	United Kingdom	Holding company
Hawthorn Asset Co Limited	United Kingdom	Securitisation entity
Hawthorn Finance Limited	Jersey	Securitisation entity
Kenrick No. 1 Holdings Limited	United Kingdom	Holding company
Kenrick No. 1 Plc	United Kingdom	Securitisation entity
Kenrick No. 2 Holdings Limited	United Kingdom	Holding company
Kenrick No. 2 Plc	United Kingdom	Securitisation entity

The Society has no shareholdings in any of the companies listed above. Unless stated otherwise above, all are incorporated in the United Kingdom and operate in Great Britain.

The assets and liabilities within Sandwell Commercial Finance No. 1 Plc have been accounted for using the fair value option available under IAS 39.

16. Intangible assets

Group	Goodwill 2017 £m	Computer software 2017 £m	Total 2017 £m	Goodwill 2016 £m	Computer software 2016 £m	Total 2016 £m
Cost						
At beginning of year	**0.6**	**19.3**	**19.9**	0.6	15.3	15.9
Additions	**-**	**7.8**	**7.8**	-	4.0	4.0
At end of year	**0.6**	**27.1**	**27.7**	0.6	19.3	19.9
Aggregate amortisation						
At beginning of year	**-**	**11.7**	**11.7**	-	8.9	8.9
Charge for the year	**-**	**2.7**	**2.7**	-	2.8	2.8
At end of year	**-**	**14.4**	**14.4**	-	11.7	11.7
Net book value at end of year	**0.6**	**12.7**	**13.3**	0.6	7.6	8.2
Net book value at beginning of year	**0.6**	**7.6**	**8.2**	0.6	6.4	7.0

Society	Goodwill 2017 £m	Computer software 2017 £m	Total 2017 £m	Goodwill 2016 £m	Computer software 2016 £m	Total 2016 £m
Cost						
At beginning of year	-	19.3	19.3	-	15.3	15.3
Additions	-	7.8	7.8	-	4.0	4.0
At end of year	-	27.1	27.1	-	19.3	19.3
Aggregate amortisation						
At beginning of year	-	11.7	11.7	-	8.9	8.9
Charge for the year	-	2.7	2.7	-	2.8	2.8
At end of year	-	14.4	14.4	-	11.7	11.7
Net book value at end of year	-	12.7	12.7	-	7.6	7.6
Net book value at beginning of year	-	7.6	7.6	-	6.4	6.4

The goodwill has been assessed as having an indefinite life. In accordance with IAS 38 'Intangible Assets', the Group carries out an annual impairment test in relation to goodwill.

The recoverable amount has been calculated with reference to future earnings and value in use. The calculations incorporate cash flow projections from the three year business plan approved by the Group Board and cash flow forecasts for the following 10 years, reflecting the enduring nature of the business concerned. The long term growth rates of 3.0% (2015/16: 3.0%) are based upon management's expectations of long-term GDP growth over the forecast period. The pre-tax rate used to discount projected cash flows is 12.5% (2015/16: 12.5%), reflecting management's estimate of the required return.

17. Investment properties

	Group 2017 £m	Group 2016 £m
Valuation		
At beginning of year	123.7	118.6
Disposals	(0.2)	(0.4)
Revaluation gains	5.4	5.5
At end of year	128.9	123.7

A national firm of specialist residential valuers, Connells Limited, has carried out a valuation review of the residential investment properties held by West Bromwich Homes Limited. This review involved a physical 'drive by' inspection of a sample of approximately 10% of the total portfolio, together with a review of desktop market value assessments and output from an automated valuation model of all remaining properties on an individual basis.

Connells Limited confirms that, based on the valuation output reviewed, it is satisfied that the overall valuation of the portfolio at 31 March 2017 is a fair reflection of market value. The valuation was prepared in accordance with the Valuation Standards issued by the Royal Institution of Chartered Surveyors (known as the 'Red Book'), in particular UK Practice Statement 1. Market value is as defined in Practice Statement 3.2. This fair value measurement is categorised as a Level 3 fair value measurement, based on an assessment of the inputs to the valuation methodology described above.

If the land and buildings were carried at cost, the carrying amount would be £84.7m (2015/16: £84.9m).

The Group leases investment properties to non-commercial individuals for a contract period of up to 12 months. The future minimum lease receipts under non-cancellable operating leases that end within 12 months are £2.7m (2015/16: £2.5m). The Group has not recognised any contingent rent in the period (2015/16: £nil).

18. Property, plant and equipment

	Land and buildings					
Group	**Freehold branches and non-specialised buildings £m**	**Specialised administration buildings £m**	**Held for sale £m**	**Short leasehold £m**	**Equipment, fixtures, fittings and vehicles £m**	**Total £m**
Cost or valuation						
At 1 April 2016	25.7	-	0.5	0.7	22.1	**49.0**
Additions	-	0.1	-	0.3	0.8	**1.2**
Transfers	(20.7)	20.7	-	-	-	**-**
Revaluation	0.4	-	-	-	-	**0.4**
Disposals	-	-	(0.5)	-	(0.1)	**(0.6)**
At 31 March 2017	**5.4**	**20.8**	**-**	**1.0**	**22.8**	**50.0**
Accumulated depreciation						
At 1 April 2016	0.3	-	-	0.6	14.2	**15.1**
Transfers	(0.1)	0.1	-	-	-	**-**
Revaluation	(0.2)	-	-	-	-	**(0.2)**
Charge for the year	-	0.8	-	-	2.2	**3.0**
At 31 March 2017	**-**	**0.9**	**-**	**0.6**	**16.4**	**17.9**
Net book value						
At 31 March 2017	**5.4**	**19.9**	**-**	**0.4**	**6.4**	**32.1**

	Land and buildings					
Group	Freehold £m	In the course of construction £m	Held for sale £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation						
At 1 April 2015	5.0	16.4	0.5	0.7	20.4	43.0
Additions	1.2	3.6	-	-	1.2	6.0
Transfers	19.5	(20.0)	-	-	0.5	-
At 31 March 2016	25.7	-	0.5	0.7	22.1	49.0
Accumulated depreciation						
At 1 April 2015	0.1	-	-	0.6	12.1	12.8
Charge for the year	0.2	-	-	-	2.1	2.3
At 31 March 2016	0.3	-	-	0.6	14.2	15.1
Net book value						
At 31 March 2016	25.4	-	0.5	0.1	7.9	33.9

Society	Land and buildings: Freehold branches and non-specialised buildings £m	Land and buildings: Specialised administration buildings £m	Land and buildings: Held for sale £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation						
At 1 April 2016	25.7	-	0.5	0.7	21.9	**48.8**
Additions	-	0.1	-	0.3	0.8	**1.2**
Transfers	(20.7)	20.7	-	-	-	**-**
Revaluation	0.4	-	-	-	-	**0.4**
Disposals	-	-	(0.5)	-	(0.1)	**(0.6)**
At 31 March 2017	**5.4**	**20.8**	**-**	**1.0**	**22.6**	**49.8**
Accumulated depreciation						
At 1 April 2016	0.3	-	-	0.6	14.0	**14.9**
Transfers	(0.1)	0.1	-	-	-	**-**
Revaluation	(0.2)	-	-	-	-	**(0.2)**
Charge for the year	-	0.8	-	-	2.2	**3.0**
At 31 March 2017	**-**	**0.9**	**-**	**0.6**	**16.2**	**17.7**
Net book value						
At 31 March 2017	**5.4**	**19.9**	**-**	**0.4**	**6.4**	**32.1**

Society	Land and buildings: Freehold £m	Land and buildings: In the course of construction £m	Land and buildings: Held for sale £m	Short leasehold £m	Equipment, fixtures, fittings and vehicles £m	Total £m
Cost or valuation						
At 1 April 2015	5.0	16.4	0.5	0.7	20.2	42.8
Additions	1.2	3.6	-	-	1.2	6.0
Transfers	19.5	(20.0)	-	-	0.5	-
At 31 March 2016	25.7	-	0.5	0.7	21.9	48.8
Accumulated depreciation						
At 1 April 2015	0.1	-	-	0.6	11.9	12.6
Charge for the year	0.2	-	-	-	2.1	2.3
At 31 March 2016	0.3	-	-	0.6	14.0	14.9
Net book value						
At 31 March 2016	25.4	-	0.5	0.1	7.9	33.9

The net book value of land and buildings occupied for the Society's own use is £25.7m (2015/16: £26.0m).

The Group's freehold branches and non-specialised buildings were revalued at 31 March 2017 by Colliers International, a firm of independent chartered surveyors. The valuations were undertaken in accordance with the Valuation Standards issued by the Royal Institution of Chartered Surveyors in the United Kingdom. These valuations have been incorporated into the financial statements and the resulting revaluation credit of £0.6m taken to the revaluation reserve.

If land and buildings were carried at historical cost, the carrying amount would be £21.2m (2015/16: £22.6m).

As part of the ongoing funding agreement for the West Bromwich Building Society Staff Retirement Scheme (the SRS), the Trustees of the SRS have been granted a charge over the Society's Head Office, a specialised administration building. The charge may be exercised only in the event of the Society defaulting on its pension obligations and in such circumstances assigns the rights of ownership of the building to the SRS.

19. Deferred tax

Deferred tax is calculated on all temporary differences under the liability method using an effective tax rate of 17% to 19% (2015/16: 18%). The movement on the deferred tax account is as follows:

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
At beginning of year	**15.7**	19.4	**12.9**	12.3
Current year Income Statement charge	**(5.6)**	(1.8)	**(4.5)**	(0.6)
Amount recognised directly in other comprehensive income	**1.0**	(0.9)	**0.9**	(1.0)
Adjustments in respect of prior years	**0.3**	(1.0)	**1.4**	2.2
At end of year	**11.4**	15.7	**10.7**	12.9

Deferred tax assets and liabilities are attributable to the following items:

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Deferred tax assets				
Accelerated tax depreciation	**5.9**	5.3	**5.9**	5.3
Carried forward tax losses	**8.9**	14.7	**4.4**	7.5
Pensions and other post retirement benefits	**1.1**	-	**1.1**	-
Other temporary differences	**0.5**	0.4	**0.3**	0.7
	16.4	20.4	**11.7**	13.5
Deferred tax liabilities				
Property valuations	**(4.2)**	(4.1)	**(0.6)**	(0.4)
Other temporary differences	**(0.8)**	(0.6)	**(0.4)**	(0.2)
	(5.0)	(4.7)	**(1.0)**	(0.6)

The deferred tax (charge)/credit in the Income Statement comprises the following temporary differences:

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Accelerated tax depreciation	**0.6**	-	**0.6**	-
Other provisions	**-**	(0.7)	**(0.5)**	(0.4)
Carried forward tax losses	**(5.8)**	(1.9)	**(3.1)**	2.0
Property valuations	**0.1**	(0.2)	**-**	-
	(5.1)	(2.8)	**(3.0)**	1.6

Deferred tax assets are recognised only to the extent that realisation of the related tax benefit against future taxable profits is probable over the foreseeable future. The deferred tax asset balances attributable to carried forward losses are expected to be substantially recovered against future taxable profits (as projected in the latest Strategic Plan) within five years. The assumptions surrounding future expected credit losses and increases in the Bank Rate of interest represent the most subjective areas of judgement in management's projections of future taxable profits. The deferred tax assets have not been discounted.

Deferred tax assets and liabilities are offset where there is a legally enforceable right to do so.

The UK corporation tax rate reduces to 19%, effective from 1 April 2017, and 17% with effect from 1 April 2020. Deferred tax assets and liabilities have been recognised at rates between 17% and 19% (2015/16: 18%), being the rates substantively enacted at the Statement of Financial Position date and expected to apply when the deferred tax balances are realised.

20. Trade and other receivables

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Prepayments and accrued income	**3.2**	2.4	**3.2**	2.4
Other	**0.3**	0.3	**0.1**	0.3
	3.5	2.7	**3.3**	2.7

21. Shares

Group and Society	2017 £m	2016 £m
Held by individuals	**4,423.2**	4,377.4
Other shares	**1.1**	1.1
Fair value adjustment for hedged risk	**3.0**	6.6
	4,427.3	4,385.1

22. Amounts due to other customers

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Deemed loans	**-**	-	**256.7**	341.3
Other customers	**132.7**	157.0	**133.6**	158.7
	132.7	157.0	**390.3**	500.0

23. Debt securities in issue

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Non-recourse finance on securitised advances	**263.2**	368.6	**-**	-

The non-recourse finance comprises mortgage backed floating rate notes (the Notes) secured over portfolios of mortgage loans secured by first charges over residential and commercial properties in the United Kingdom (see note 13). Prior to redemption of the Notes on the final interest payment dates, the Notes will be subject to mandatory and/or optional redemption, in certain circumstances, on each interest payment date. See note 28 for details of assets and liabilities held at fair value through profit or loss.

24. Trade and other payables

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Accruals	**7.2**	7.9	**6.7**	7.6
Other creditors	**3.0**	4.7	**2.7**	4.0
Income tax	**-**	2.6	**-**	2.6
	10.2	15.2	**9.4**	14.2

25. Provisions for liabilities

Group	**Buy to let 2017 £m**	**FSCS 2017 £m**	**Onerous contracts 2017 £m**	**Other 2017 £m**	**Total 2017 £m**
At beginning of year	**-**	**1.4**	**0.1**	**1.2**	**2.7**
Utilised in the year	**(27.5)**	**(1.4)**	**(0.1)**	**(0.5)**	**(29.5)**
Charge for the year	**27.5**	**0.8**	**-**	**1.6**	**29.9**
At end of year	**-**	**0.8**	**-**	**2.3**	**3.1**

Group	Buy to let 2016 £m	FSCS 2016 £m	Onerous contracts 2016 £m	Other 2016 £m	Total 2016 £m
At beginning of year	-	1.8	-	0.4	2.2
Utilised in the year	-	(3.0)	-	(0.5)	(3.5)
Charge for the year	-	2.6	0.1	1.3	4.0
At end of year	-	1.4	0.1	1.2	2.7

Society	**Buy to let 2017 £m**	**FSCS 2017 £m**	**Onerous contracts 2017 £m**	**Other 2017 £m**	**Total 2017 £m**
At beginning of year	**-**	**1.4**	**0.1**	**1.1**	**2.6**
Utilised in the year	**-**	**(1.4)**	**(0.1)**	**(0.4)**	**(1.9)**
Charge for the year	**-**	**0.8**	**-**	**1.5**	**2.3**
At end of year	**-**	**0.8**	**-**	**2.2**	**3.0**

Society	Buy to let 2016 £m	FSCS 2016 £m	Onerous contracts 2016 £m	Other 2016 £m	Total 2016 £m
At beginning of year	-	1.8	-	0.1	1.9
Utilised in the year	-	(3.0)	-	(0.3)	(3.3)
Charge for the year	-	2.6	0.1	1.3	4.0
At end of year	-	1.4	0.1	1.1	2.6

Buy to let provision

In December 2013, West Bromwich Mortgage Company (the Company) chose to vary the interest rate margin charged for certain multi-property landlords in line with the terms and conditions of their buy to let mortgages. Certain impacted parties initiated legal proceedings against the Company to challenge this increase. Following a successful defence of this challenge in the High Court a final judgement was made in the Court of Appeal in June 2016 which ruled against the Company. During 2016/17, the interest rate variation applied since December 2013 has been refunded in full to all buy to let borrowers affected.

Financial Services Compensation Scheme (FSCS)

In common with all regulated UK deposit takers, the Society pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. The FSCS levy consists of two parts: a management expenses levy and a compensation levy. The management expenses levy covers the costs of running the scheme and the compensation levy covers the amount of compensation the scheme pays, net of any recoveries it makes.

The provision at 31 March 2017 represents the estimated management expenses levy due for the scheme year 2016/17. This provision was calculated based on the Society's share of protected deposits and the FSCS estimate of total management expenses for the scheme year.

Onerous contracts

The provision for onerous contracts covers the loss anticipated in connection with future lease expenses from non-cancellable lease commitments in branches that the Society has, as part of its branch restructure, decided are no longer required.

Other provisions

Other provisions primarily relate to Payment Protection Insurance (PPI) redress and represent the amounts expected to be settled based on an anticipated deadline for PPI claims of August 2019. Following the Supreme Court's decision in the case of Plevin v Paragon Personal Finance Limited, the Financial Conduct Authority (FCA) has sought to define circumstances whereby the levels of commission earned on PPI sales gave rise to a potentially 'unfair relationship'. The PPI provision incorporates the Society's expected obligations under the new FCA rules and guidelines.

26. Subscribed capital

Group and Society	2017 £m	2016 £m
Permanent interest bearing shares	**75.0**	74.9

In a winding up or dissolution of the Society the claims of the holders of permanent interest bearing shares (PIBS) would rank behind all other creditors of the Society, with the exception of the claims of holders of profit participating deferred shares (PPDS) with which the PIBS rank pari-passu, and the claims of members holding shares as to principal and interest. The holders of PIBS are not entitled to any share in any final surplus upon winding up or dissolution of the Society.

With respect to future interest payments, as a condition of the PPDS (see note 27), the Society has undertaken to pay an amount which, when annualised, represents the lower of: 6.15% of the outstanding principal amount of the PIBS and the dividend yield attributable to the PPDS with respect to the prior financial year ending 31 March whose payment is at the discretion of the Society.

27. Profit participating deferred shares

Group and Society	2017 £m	2016 £m
Book value		
Nominal value	**182.5**	182.5
Cumulative fair value adjustments at date of transition	**3.8**	3.8
Capitalised issue costs	**(2.2)**	(2.2)
	184.1	184.1
Cumulative reserve deficit		
At beginning of year	**(4.6)**	(7.0)
Share of (loss)/profit for the financial year	**(6.5)**	2.4
	(11.1)	(4.6)
Net value at end of year	**173.0**	179.5

The profit participating deferred shares (PPDS) are entitled to receive a distribution, at the discretion of the Society, of up to 25% of the Group's post-tax profits in the future (calculated prior to payment of the PPDS dividend). No such distribution may be made if the PPDS cumulative reserves are in deficit.

28. Financial assets and liabilities at fair value through profit or loss

Financial assets and liabilities are designated at fair value through profit or loss when this results in more relevant information because it significantly reduces a measurement inconsistency that would otherwise arise from measuring assets or liabilities or recognising the gains and losses on them on different bases. The 'fair value option' is used by the Group where financial assets or liabilities would otherwise be measured at amortised cost, the associated derivatives used to economically hedge the risk are held at fair value, and it is not practical to apply hedge accounting. The table below shows the carrying value of financial assets and liabilities that upon initial recognition, or at 1 April 2005 on the adoption of IAS 39, were designated at fair value through profit or loss, and the net gains or losses on these instruments:

	Group 2017 £m	Group 2016 £m
Financial assets at fair value through profit or loss		
Loans fully secured on land		
Carrying value at 31 March	**18.3**	23.6
Net losses in the year	**(0.1)**	(0.5)
Financial liabilities at fair value through profit or loss		
Non-recourse finance on securitised advances		
Carrying value at 31 March	**17.4**	21.8
Net losses in the year	**(0.2)**	-
Derivative financial instruments		
Carrying value at 31 March	**(2.7)**	(3.0)
Net gains in the year	**0.3**	0.5

29. Tax effects relating to each component of other comprehensive income

Group	**Before tax amount 2017 £m**	**Taxation 2017 £m**	**Net of tax amount 2017 £m**
Actuarial losses on defined benefit obligations	**(10.4)**	**1.9**	**(8.5)**
Revaluation reserve	**0.6**	**(0.2)**	**0.4**
Amortisation of original discount on subscribed capital	**0.1**	**-**	**0.1**
Cash flow hedges	**(0.5)**	**0.1**	**(0.4)**
Other comprehensive income	**(10.2)**	**1.8**	**(8.4)**

Group	Before tax amount 2016 £m	Taxation 2016 £m	Net of tax amount 2016 £m
Available for sale financial assets	(2.8)	0.2	(2.6)
Actuarial losses on defined benefit obligations	(0.9)	0.1	(0.8)
Cash flow hedges	(0.2)	-	(0.2)
Other comprehensive income	(3.9)	0.3	(3.6)

Society	**Before tax amount 2017 £m**	**Taxation 2017 £m**	**Net of tax amount 2017 £m**
Actuarial losses on defined benefit obligations	**(10.4)**	**1.9**	**(8.5)**
Revaluation reserve	**0.6**	**(0.2)**	**0.4**
Amortisation of original discount on subscribed capital	**0.1**	**-**	**0.1**
Other comprehensive income	**(9.7)**	**1.7**	**(8.0)**

Society	Before tax amount 2016 £m	Taxation 2016 £m	Net of tax amount 2016 £m
Available for sale financial assets	(2.8)	0.2	(2.6)
Actuarial losses on defined benefit obligations	(0.9)	0.1	(0.8)
Other comprehensive income	(3.7)	0.3	(3.4)

30. Retirement benefit obligations

Group and Society	2017 £m	2016 £m	2015 £m	2014 £m	2013 £m
Defined benefit pension scheme obligation/(asset)	**6.5**	(0.8)	7.5	1.4	(0.4)

Defined benefit plans

The Society operates the West Bromwich Building Society Staff Retirement Scheme (SRS), a funded pension scheme providing benefits for some of its employees based on final pensionable emoluments. The assets of the scheme are held in a separate trustee administered fund. In addition, the Society has some unregistered arrangements in place in respect of former Directors. The financial effect of these arrangements is included in this note.

The results of a formal actuarial valuation at 31 March 2016 carried out by the appointed actuary to the scheme were updated to the accounting date by an independent qualified actuary in accordance with IAS 19, 'Employee Benefits'.

The Society closed the scheme to the future accrual of benefits with effect from 1 August 2009, at which date all previously active members became entitled to deferred pensions in the scheme.

As part of the ongoing funding agreement for the SRS, the Trustees of the SRS have been granted a charge over the Society's Head Office, which may be exercised only in the event of the Society defaulting on its pension obligations and in such circumstances assigns the rights of ownership of the building to the SRS.

The scheme is subject to the funding legislation outlined in the Pensions Act 2004 which came into force on 30 December 2005. This, together with documents issued by the Pensions Regulator, and Guidance Notes adopted by the Financial Reporting Council, sets out the framework for funding defined benefit occupational pension schemes in the UK.

IAS 19 allows an employer to recognise a surplus as an asset to the extent that it is able to recover a surplus either through reduced contributions in the future or through refunds from the scheme, even if the refunds may only be available at some distant time in the future, such as after the last benefit has been paid.

The key assumptions used by the actuary in the updated calculation were:

Group and Society	2017	2016	2015	2014	2013
Pension increases in payment (RPI capped at 5%)	**3.1%**	2.8%	2.8%	3.3%	3.3%
Pension increases in payment (CPI capped at 2.5%)	**1.7%**	1.6%	1.6%	2.0%	2.0%
Discount rate	**2.8%**	3.7%	3.5%	4.6%	4.4%
Life expectancy of male aged 65 at year end date	**23.2**	23.0	22.9	22.9	22.3
Life expectancy of female aged 65 at year end date	**24.2**	24.4	24.3	24.2	23.7
Life expectancy of male aged 65 at year end date plus 20 years	**25.0**	24.4	24.3	24.2	24.6
Life expectancy of female aged 65 at year end date plus 20 years	**26.1**	25.9	25.8	25.7	26.1

The sensitivity of the defined benefit obligation to changes in the significant actuarial assumptions is shown in the table below:

Group and Society	2017 £m	2016 £m
Discount rate		
Effect on defined benefit obligation of a 1% increase	**(20.3)**	(15.8)
Inflation		
Effect on defined benefit obligation of a 1% increase	**16.8**	13.3
Life expectancy		
Effect on defined benefit obligation of a 1 year increase	**3.4**	2.8

30. Retirement benefit obligations (continued)

The amounts recognised in the Statement of Financial Position are as follows:

Group and Society	2017 £m	2016 £m	2015 £m	2014 £m	2013 £m
Present value of funded obligations	**113.2**	93.6	97.8	85.1	87.9
Present value of unfunded obligations	**0.8**	0.6	1.0	0.9	0.9
	114.0	94.2	98.8	86.0	88.8
Fair value of scheme assets	**(107.5)**	(95.0)	(91.3)	(84.6)	(89.2)
Net liability/(asset) in the Statement of Financial Position	**6.5**	(0.8)	7.5	1.4	(0.4)

The amounts recognised in the Income Statement are as follows:

Group and Society	2017 £m	2016 £m	2015 £m
Interest cost	**3.4**	3.4	3.9
Interest receivable on plan assets	**(3.4)**	(3.3)	(3.9)
Running costs	**0.3**	0.2	0.2
Total pension fund cost	**0.3**	0.3	0.2

Running costs, other than those associated with management of scheme assets, are shown in administrative expenses whilst interest cost and interest receivable on plan assets are disclosed as other operating income.

Change in benefit obligations

Group and Society	2017 £m	2016 £m	2015 £m
Benefit obligations at beginning of year	**94.2**	98.8	86.0
Interest cost	**3.4**	3.4	3.9
Actuarial losses/(gains)	**21.0**	(5.2)	12.2
Running costs (release of reserve)	**(0.1)**	(0.1)	(0.1)
Benefits paid	**(4.5)**	(2.7)	(3.2)
Benefit obligations at end of year	**114.0**	94.2	98.8

Change in scheme assets

Group and Society	2017 £m	2016 £m	2015 £m
Fair value of scheme assets at beginning of year	**95.0**	91.3	84.6
Interest receivable on plan assets	**3.4**	3.3	3.9
Actuarial gains/(losses)	**10.6**	(6.1)	1.5
Contribution by employer	**3.4**	9.5	4.8
Running costs	**(0.4)**	(0.3)	(0.3)
Benefits paid	**(4.5)**	(2.7)	(3.2)
Fair value of scheme assets at end of year	**107.5**	95.0	91.3

The amount recognised outside profit and loss in the Statement of Comprehensive Income for 2016/17 is an actuarial loss of £10.4m (2015/16: £0.9m). The cumulative amount recognised outside profit and loss at 31 March 2017 is an actuarial loss of £53.6m.

History of experience gains and losses

Group and Society	2017	2016	2015	2014	2013
Experience gains/(losses) on scheme assets:					
Amount (£m)	**10.6**	(6.1)	1.5	(9.9)	5.8
Percentage of scheme assets	**10%**	(6%)	2%	(12%)	7%
Experience (gains)/losses on scheme liabilities:					
Amount (£m)	**(0.9)**	(1.7)	(1.3)	(0.4)	(0.2)
Percentage of scheme liabilities	**(1%)**	(2%)	(1%)	(0%)	(0%)

Scheme assets

Provisional asset information at bid value was supplied by the investment managers. The value of the invested assets at 31 March 2017 was £107.5m, analysed as follows:

Group and Society	2017 £m	2016 £m	2015 £m
Diversified growth fund	**54.2**	53.5	51.8
Liability driven investment	**28.6**	23.6	19.2
Insurance asset	**19.4**	17.2	18.4
Cash and other assets	**5.3**	0.7	1.9
	107.5	95.0	91.3

As part of its asset and liability matching investment strategy, designed to mitigate inflation and interest rate risk exposure, the Scheme has invested in three pooled liability driven investment funds. In addition, an insurance policy has been purchased to provide income which provides a specific match against the liabilities arising from a large proportion of the Scheme's current pensioners.

With a view to reducing the investment risk within the Scheme's asset portfolio, a large proportion of the investments are now held in Diversified Growth Funds (DGFs), rather than direct equity funds. Although DGFs do themselves include equity investments this is part of a more diversified strategy which is expected to reduce overall investment volatility whilst still maintaining relatively strong returns.

Stakeholder scheme

The total cost for the year of the stakeholder plan to the Group and Society was £1.0m (2015/16: £1.0m) and there were no outstanding contributions at the end of the year (2015/16: £nil).

For the period through to 31 July 2009 staff could contribute between 2% and 9% with the Society contributing on a sliding scale between 2% and 7%. From 1 August 2009 staff have been able to contribute between 2% and 10% with the Society providing matched funding.

31. Financial instruments

A financial instrument is a contract that gives rise to a financial asset of one entity and a financial liability or equity of another entity.

The Group is a retailer of financial instruments, mainly in the form of mortgages and savings. The Group uses wholesale financial instruments to invest liquid asset balances and raise wholesale funding, and to manage the risks arising from its operations. As a result of these activities, the Group is exposed to a variety of risks, the most significant of which are credit risk, liquidity risk and market risk (principally interest rate and equity risk). These risks are described in notes 32 to 34.

The use of derivative financial instruments for risk management purposes is described in note 33.

Classification of financial assets and financial liabilities

The following tables show the classification of the Group's and Society's financial assets and liabilities:

At 31 March 2017

Group	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	294.8	-	-	**294.8**
Loans and advances to credit institutions	174.0	-	-	**174.0**
Investment securities	-	385.0	-	**385.0**
Derivative financial instruments	-	-	6.3	**6.3**
Loans and advances to customers	4,758.2	-	18.3	**4,776.5**
Total financial assets	**5,227.0**	**385.0**	**24.6**	**5,636.6**
Non-financial assets				**194.2**
Total assets				**5,830.8**

	Other financial liabilities £m	Fair value through profit or loss £m	Total £m
Liabilities			
Shares	4,427.3	-	**4,427.3**
Amounts due to credit institutions	450.3	-	**450.3**
Amounts due to other customers	132.7	-	**132.7**
Derivative financial instruments	-	69.0	**69.0**
Debt securities in issue	245.8	17.4	**263.2**
Total financial liabilities	**5,256.1**	**86.4**	**5,342.5**
Non-financial liabilities			**24.8**
Total liabilities			**5,367.3**

At 31 March 2016

Group	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	215.4	-	-	215.4
Loans and advances to credit institutions	204.0	-	-	204.0
Investment securities	-	410.1	-	410.1
Derivative financial instruments	-	-	8.9	8.9
Loans and advances to customers	4,715.4	-	23.6	4,739.0
Total financial assets	5,134.8	410.1	32.5	5,577.4
Non-financial assets				189.7
Total assets				5,767.1
		Other financial liabilities £m	Fair value through profit or loss £m	Total £m
Liabilities				
Shares		4,385.1	-	4,385.1
Amounts due to credit institutions		259.0	-	259.0
Amounts due to other customers		157.0	-	157.0
Derivative financial instruments		-	77.1	77.1
Debt securities in issue		346.8	21.8	368.6
Total financial liabilities		5,147.9	98.9	5,246.8
Non-financial liabilities				22.6
Total liabilities				5,269.4

31. Financial instruments (continued)

Classification of financial assets and financial liabilities (continued)

At 31 March 2017

Society	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	294.8	-	-	**294.8**
Loans and advances to credit institutions	91.7	-	-	**91.7**
Investment securities	810.5	385.0	-	**1,195.5**
Derivative financial instruments	-	-	6.2	**6.2**
Loans and advances to customers	2,663.7	-	-	**2,663.7**
Investments	1,526.9	-	-	**1,526.9**
Total financial assets	**5,387.6**	**385.0**	**6.2**	**5,778.8**
Non-financial assets				**59.8**
Total assets				**5,838.6**

	Other financial liabilities £m	Fair value through profit or loss £m	Total £m
Liabilities			
Shares	4,427.3	-	**4,427.3**
Amounts due to credit institutions	450.3	-	**450.3**
Amounts due to other customers	390.3	-	**390.3**
Derivative financial instruments	-	59.7	**59.7**
Total financial liabilities	**5,267.9**	**59.7**	**5,327.6**
Non-financial liabilities			**19.9**
Total liabilities			**5,347.5**

At 31 March 2016

Society	Amortised cost £m	Available for sale £m	Fair value through profit or loss £m	Total £m
Assets				
Cash and balances with the Bank of England	215.4	-	-	215.4
Loans and advances to credit institutions	93.2	-	-	93.2
Investment securities	889.9	410.1	-	1,300.0
Derivative financial instruments	-	-	8.8	8.8
Loans and advances to customers	2,380.1	-	-	2,380.1
Investments	1,669.2	-	-	1,669.2
Total financial assets	5,247.8	410.1	8.8	5,666.7
Non-financial assets				58.5
Total assets				5,725.2

	Other financial liabilities £m	Fair value through profit or loss £m	Total £m
Liabilities			
Shares	4,385.1	-	4,385.1
Amounts due to credit institutions	259.0	-	259.0
Amounts due to other customers	500.0	-	500.0
Derivative financial instruments	-	67.4	67.4
Total financial liabilities	5,144.1	67.4	5,211.5
Non-financial liabilities			17.4
Total liabilities			5,228.9

The Group and Society financial assets and liabilities recorded at fair value through profit or loss consist of derivative financial instruments and instruments that were designated as such upon initial recognition to avoid an accounting mismatch. As discussed in notes 1 and 28, these are economically hedged where it is not practical to apply hedge accounting.

31. Financial instruments (continued)

Fair values of financial assets and financial liabilities

Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. The Group determines fair values by the following three tier valuation hierarchy:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.

Level 2: Valuation techniques where all inputs are taken from observable market data, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3: Valuation techniques where significant inputs are not based on observable market data.

Valuation techniques include net present value and discounted cash flow models, comparison to similar instruments for which market observable prices exist and other valuation models. Assumptions and market observable inputs used in valuation techniques include risk-free and benchmark interest rates, equity index prices and expected price volatilities. The objective of valuation techniques is to arrive at a fair value determination that reflects the price of the financial instrument at the reporting date that would have been determined by market participants acting at arm's length. Observable prices are those that have been seen either from counterparties or from market pricing sources including Bloomberg. The use of these depends upon the liquidity of the relevant market.

Financial assets and financial liabilities held at amortised cost

The tables below show the fair values of the Group's and Society's financial assets and liabilities held at amortised cost in the Statements of Financial Position, analysed according to the fair value hierarchy described above.

At 31 March 2017

Group	Carrying value £m	Fair value Level 1 £m	Fair value Level 2 £m	Fair value Level 3 £m	Fair value Total £m
Financial assets					
Cash and balances with the Bank of England	**294.8**	294.8	-	-	**294.8**
Loans and advances to credit institutions	**174.0**	-	174.0	-	**174.0**
Loans and advances to customers	**4,758.2**	-	-	4,790.0	**4,790.0**
	5,227.0	**294.8**	**174.0**	**4,790.0**	**5,258.8**
Financial liabilities					
Shares	**4,427.3**	-	-	4,416.6	**4,416.6**
Amounts due to credit institutions	**450.3**	-	450.3	-	**450.3**
Amounts due to other customers	**132.7**	-	132.7	-	**132.7**
Debt securities in issue	**245.8**	230.0	8.2	-	**238.2**
	5,256.1	**230.0**	**591.2**	**4,416.6**	**5,237.8**

At 31 March 2016

Group	Carrying value £m	Fair value Level 1 £m	Fair value Level 2 £m	Fair value Level 3 £m	Fair value Total £m
Financial assets					
Cash and balances with the Bank of England	215.4	215.4	-	-	215.4
Loans and advances to credit institutions	204.0	-	204.0	-	204.0
Loans and advances to customers	4,715.4	-	-	4,684.7	4,684.7
	5,134.8	215.4	204.0	4,684.7	5,104.1
Financial liabilities					
Shares	4,385.1	-	-	4,371.6	4,371.6
Amounts due to credit institutions	259.0	-	259.0	-	259.0
Amounts due to other customers	157.0	-	157.0	-	157.0
Debt securities in issue	346.8	329.9	8.1	-	338.0
	5,147.9	329.9	424.1	4,371.6	5,125.6

At 31 March 2017

Society	Carrying value £m	Fair value Level 1 £m	Fair value Level 2 £m	Fair value Level 3 £m	Fair value Total £m
Financial assets					
Cash and balances with the Bank of England	**294.8**	294.8	-	-	**294.8**
Loans and advances to credit institutions	**91.7**	-	91.7	-	**91.7**
Investment securities	**810.5**	56.2	753.3	-	**809.5**
Loans and advances to customers	**2,663.7**	-	-	2,711.1	**2,711.1**
	3,860.7	**351.0**	**845.0**	**2,711.1**	**3,907.1**
Financial liabilities					
Shares	**4,427.3**	-	-	4,416.6	**4,416.6**
Amounts due to credit institutions	**450.3**	-	450.3	-	**450.3**
Amounts due to other customers	**390.3**	-	390.3	-	**390.3**
	5,267.9	**-**	**840.6**	**4,416.6**	**5,257.2**

At 31 March 2016

Society	Carrying value £m	Fair value Level 1 £m	Fair value Level 2 £m	Fair value Level 3 £m	Fair value Total £m
Financial assets					
Cash and balances with the Bank of England	215.4	215.4	-	-	215.4
Loans and advances to credit institutions	93.2	-	93.2	-	93.2
Investment securities	889.9	58.6	830.5	-	889.1
Loans and advances to customers	2,380.1	-	-	2,404.0	2,404.0
	3,578.6	274.0	923.7	2,404.0	3,601.7
Financial liabilities					
Shares	4,385.1	-	-	4,371.6	4,371.6
Amounts due to credit institutions	259.0	-	259.0	-	259.0
Amounts due to other customers	500.0	-	500.0	-	500.0
	5,144.1	-	759.0	4,371.6	5,130.6

31. Financial instruments (continued)

a) Loans and advances to customers
The fair value of loans and advances to customers has been determined taking into account factors such as impairment and interest rates. The fair values have been calculated on a product basis and as such do not necessarily represent the value that could have been obtained for a portfolio if it were sold at 31 March 2017.

b) Shares and borrowings
The estimated fair value of deposits with no stated maturity, which includes non-interest bearing deposits, is the amount repayable on demand. The estimated fair value of fixed interest-bearing deposits and other borrowings without quoted market price is based on discounted cash flows using interest rates for new deposits with similar remaining maturity. The fair values have been calculated on a product basis and as such do not necessarily represent the value that could have been obtained for a portfolio if it were sold at 31 March 2017.

c) Debt securities in issue
The aggregate fair values are calculated based on quoted market prices. For those notes where quoted market prices are not available, a discounted cash flow model is used based on a current yield curve appropriate for the remaining term to maturity.

Financial assets and financial liabilities held at fair value through profit or loss

The tables below show the fair values of the Group's and Society's financial assets and liabilities held at fair value in the Statements of Financial Position, analysed according to the fair value hierarchy described previously.

Group	Level 1 2017 £m	Level 2 2017 £m	Total 2017 £m
Financial assets			
Investment securities	385.0	-	**385.0**
Derivative financial instruments	-	6.3	**6.3**
Loans and advances to customers	-	18.3	**18.3**
	385.0	**24.6**	**409.6**
Financial liabilities			
Derivative financial instruments	-	69.0	**69.0**
Debt securities in issue	-	17.4	**17.4**
	-	**86.4**	**86.4**

Group	Level 1 2016 £m	Level 2 2016 £m	Total 2016 £m
Financial assets			
Investment securities	359.0	51.1	410.1
Derivative financial instruments	-	8.9	8.9
Loans and advances to customers	-	23.6	23.6
	359.0	83.6	442.6
Financial liabilities			
Derivative financial instruments	-	77.1	77.1
Debt securities in issue	-	21.8	21.8
	-	98.9	98.9

Society	**Level 1 2017 £m**	**Level 2 2017 £m**	**Total 2017 £m**
Financial assets			
Investment securities	385.0	-	**385.0**
Derivative financial instruments	-	6.2	**6.2**
	385.0	**6.2**	**391.2**
Financial liabilities			
Derivative financial instruments	-	59.7	**59.7**
	-	**59.7**	**59.7**

Society	Level 1 2016 £m	Level 2 2016 £m	Total 2016 £m
Financial assets			
Investment securities	359.0	51.1	410.1
Derivative financial instruments	-	8.8	8.8
	359.0	59.9	418.9
Financial liabilities			
Derivative financial instruments	-	67.4	67.4
	-	67.4	67.4

32. Credit risk

Credit risk can be described as the risk of customers or counterparties being unable to meet their financial obligations to the Group as they become due.

The Group is exposed to this risk through its lending to:

- individuals (consumers - residential mortgages, including buy to let);
- businesses (non-consumers - previous commercial lending and elements of buy to let exposure). The Group ceased new commercial lending and buy to let in 2008/9; and
- wholesale counterparties (including other financial institutions). Specifically within the treasury portfolio assets, where credit risk arises from the investments held by the Group in order to meet liquidity requirements and for general business purposes.

Changes in the credit quality and the recoverability of loans and amounts due from counterparties influence the Group's exposure to credit risk. Adverse changes in the credit quality of counterparties, collateral values or deterioration in the wider economy, including rising unemployment, worsening household finances and tightening in the UK property market, resulting in declining property values, could affect the recoverability and value of the Group's assets and influence its financial performance. An economic downturn and future falls in property values (either residential or commercial) could affect the level of impairment losses currently recognised.

The controlled management of credit risk is critical to the Group's overall strategy. The Group has therefore embedded a comprehensive and robust credit risk management framework with clear lines of accountability and oversight as part of its overall governance framework. The Group has effective policies and procedures to identify, measure, monitor, manage and report credit risk within the Group's risk appetite.

The Risk Committee is responsible for the oversight of credit risk appetite that has been established by the Board and for approving lending policy and setting limits on credit exposures, which are monitored and reviewed on a monthly basis. The minutes of this committee are presented to the Board. This committee is supported by three Executive sub-committees; the Executive Risk Committee, the Residential Credit Committee and the Commercial Loans Risk Committee. Their role in the credit risk framework is outlined below:

- The Executive Risk Committee (ERC) is responsible for providing the Risk Committee with an enterprise wide view of the risk profile of the Society including current and potential risks. The ERC is also accountable for driving the detailed implementation of the Society's Risk Management Framework. In the context of credit risk the ERC proposes to Risk Committee any recommendations for Board approval regarding the Residential Lending Statement, Credit Risk Appetite Statement and Lending and Security Policies.
- The Residential Credit Committee is responsible for the monitoring of the Group's residential credit exposures and approving changes to the credit scoring systems that are utilised. In addition, the Committee reviews the type and quality of approved residential mortgage business and appraises actual arrears and repossession levels against trends and industry averages. A summary of the minutes of this committee are presented to the ERC.
- The Commercial Loans Risk Committee reviews individual commercial loans at levels mandated by the Board. This may involve reviewing individual cases on a quarterly, half yearly or annual basis.

The Group adopts a responsible approach to lending ensuring that loans are, and are expected to remain, affordable.

The maximum credit risk exposure is the carrying value as shown in the tables on pages 86 to 87. The Group's most significant exposures to credit risk are loans secured on UK residential properties and loans secured on UK land.

Residential assets

Concentration by loan type	**Group 2017 £m**	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Prime owner occupied	**2,349.6**	2,045.6	**2,178.3**	1,850.4
Buy to let	**1,803.6**	1,974.7	**446.0**	488.4
Other	**81.9**	90.9	**1.6**	1.9
Gross balances	**4,235.1**	4,111.2	**2,625.9**	2,340.7
Impairment provisions	**(16.3)**	(20.8)	**(8.8)**	(10.6)
Fair value adjustments	**9.6**	13.0	**9.6**	12.4
	4,228.4	4,103.4	**2,626.7**	2,342.5

The table below shows the geographic spread of the residential loan portfolio at the year end date:

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
East Anglia	**122.7**	110.7	**73.2**	56.2
East Midlands	**415.3**	380.7	**265.7**	215.2
Greater London	**553.6**	591.2	**240.9**	243.7
Northern Ireland	**5.2**	5.8	**0.9**	1.1
North	**164.2**	147.7	**103.9**	83.8
North West	**496.1**	460.8	**312.9**	261.9
Scotland	**116.2**	126.8	**34.8**	40.3
South East	**751.7**	742.1	**458.5**	413.1
South West	**353.4**	336.5	**229.1**	195.8
Wales	**207.6**	194.7	**131.6**	112.3
West Midlands	**705.7**	713.1	**559.5**	554.0
Yorkshire	**343.4**	301.1	**214.9**	163.3
	4,235.1	4,111.2	**2,625.9**	2,340.7

The table below shows analysis of the indexed loan to value distribution of the residential loan portfolio at the year end date:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
>95%	74.3	78.8	36.9	34.8
90% - 95%	73.8	166.4	45.9	84.4
85% - 90%	200.1	326.3	126.4	125.5
75% - 85%	720.0	765.9	367.5	400.2
50% - 75%	2,155.1	1,930.8	1,328.2	1,096.8
<50%	1,011.8	843.0	721.0	599.0
	4,235.1	4,111.2	2,625.9	2,340.7

The Group's average indexed loan to value at the year end date is 55.7% (2015/16: 59.9%).

The table below provides further information on the Group's residential loans and advances to customers by payment due status at 31 March 2017:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Loans neither past due or impaired	4,156.1	4,001.5	2,578.9	2,283.9
Past due but not impaired				
Past due 1 to 3 months	21.5	35.8	9.0	12.3
Impaired				
Not past due but impaired	20.4	21.8	20.4	21.8
Past due 1 to 3 months	1.9	0.8	0.6	-
Past due 3 to 6 months	12.5	16.2	5.0	6.3
Past due 6 to 12 months	6.5	16.0	4.2	6.7
Past due over 12 months	3.4	8.1	1.3	3.1
Possessions	12.8	11.0	6.5	6.6
	4,235.1	4,111.2	2,625.9	2,340.7

The following table indicates collateral held against residential loans and advances to customers:

Fair value of collateral held	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Not impaired	8,132.6	7,604.8	5,276.9	4,541.2
Impaired	92.0	92.5	42.7	52.5
Possessions	13.7	10.4	6.2	5.6
	8,238.3	7,707.7	5,325.8	4,599.3

The collateral held consists of properties included within the above categories. The use of such collateral is in line with terms that are usual and customary to standard lending activities.

32. Credit risk (continued)

Forbearance strategies and renegotiated loans

A range of forbearance strategies is employed in order to work with borrowers to control arrears and, wherever possible, avoid repossession. These are set out in the relevant Group policies. The agreed strategy will reflect the customer's individual circumstances and will be used in line with industry guidance. Forbearance arrangements include extended payment terms, a reduction in interest or principal repayments, and approved external debt management plans.

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

Group	Arrangements 2017 £m	Concessions 2017 £m	Capitalisation 2017 £m	Short-term interest only conversions 2017 £m	Term extensions 2017 £m	Total 2017 £m
Loans neither past due or impaired	1.7	0.2	3.3	-	2.9	**8.1**
Past due but not impaired						
Past due 1 to 3 months	2.9	0.4	-	-	-	**3.3**
Impaired						
Past due 1 to 3 months	0.5	-	-	-	-	**0.5**
Past due 3 to 6 months	5.1	0.1	-	-	0.1	**5.3**
Past due 6 to 12 months	2.8	-	-	-	0.3	**3.1**
Past due over 12 months	1.7	-	-	0.1	0.2	**2.0**
	14.7	**0.7**	**3.3**	**0.1**	**3.5**	**22.3**

Group	Arrangements 2016 £m	Concessions 2016 £m	Capitalisation 2016 £m	Short-term interest only conversions 2016 £m	Term extensions 2016 £m	Total 2016 £m
Loans neither past due or impaired	2.1	0.7	2.3	-	10.6	15.7
Past due but not impaired						
Past due 1 to 3 months	4.3	0.7	0.2	-	0.2	5.4
Impaired						
Not past due but impaired	-	-	0.1	-	0.1	0.2
Past due 1 to 3 months	0.1	0.2	0.1	-	0.2	0.6
Past due 3 to 6 months	6.0	0.4	0.2	-	0.2	6.8
Past due 6 to 12 months	7.0	0.3	0.3	-	0.2	7.8
Past due over 12 months	2.2	-	-	0.2	-	2.4
	21.7	2.3	3.2	0.2	11.5	38.9

Commercial assets

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Concentration by loan type				
Loans secured on commercial property	**524.5**	610.4	**13.8**	13.8
Loans secured on residential property	**18.7**	20.2	**16.6**	16.6
Gross balances	**543.2**	630.6	**30.4**	30.4
Impairment provisions	**(39.4)**	(43.9)	**-**	-
Fair value adjustments	**44.3**	49.0	**6.6**	7.2
	548.1	635.7	**37.0**	37.6

Of the fair value adjustments, £40.7m (2015/16: £48.7m) relate to loans secured on commercial property and £3.6m (2015/16: £4.2m) relate to loans secured on residential property.

The analysis of loans secured on commercial property by industry type is as follows:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Healthcare and leisure	**139.4**	167.0	**-**	-
Industrial and warehouse	**23.3**	23.1	**3.5**	3.5
Office	**35.1**	48.7	**4.0**	4.0
Retail	**305.4**	350.2	**6.3**	6.3
Other	**21.3**	21.4	**-**	-
	524.5	610.4	**13.8**	13.8

The table below shows the geographic spread of the commercial loan portfolio at the year end date:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
East Anglia	**13.8**	14.5	**0.1**	0.1
East Midlands	**36.7**	38.4	**2.0**	2.0
Greater London	**59.1**	74.1	**19.1**	19.1
North	**34.6**	41.7	**-**	-
North West	**178.7**	202.7	**3.5**	3.5
Scotland	**12.0**	16.8	**0.9**	0.9
South East	**79.2**	93.3	**1.4**	1.4
South West	**21.4**	24.4	**0.1**	0.1
Wales	**14.3**	18.7	**0.5**	0.5
West Midlands	**49.2**	59.7	**-**	-
Yorkshire	**44.2**	46.3	**2.8**	2.8
	543.2	630.6	**30.4**	30.4

The Group's average indexed loan to value at the year end date is 79.5% (2015/16: 82.9%).

32. Credit risk (continued)

The table below provides further information on the Group's commercial assets by payment due status at 31 March 2017:

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
Loans neither past due or impaired	**340.2**	358.4	**30.4**	30.4
Not past due but impaired	**69.6**	136.3	**-**	-
Past due but not impaired				
Past due up to 3 months	**2.8**	4.9	**-**	-
Impaired				
Past due up to 3 months	**20.6**	5.0	**-**	-
Past due 3 to 6 months	**4.6**	6.5	**-**	-
Past due 6 to 12 months	**21.1**	11.1	**-**	-
Past due over 12 months	**84.3**	108.4	**-**	-
	543.2	630.6	**30.4**	30.4

The following table indicates collateral held against commercial loans and advances to customers:

Group **Value of collateral held**	Indexed 2017 £m	Unindexed 2017 £m	Indexed 2016 £m	Unindexed 2016 £m
Not impaired	**477.0**	**424.4**	503.6	438.6
Impaired	**97.7**	**88.4**	192.4	170.2
	574.7	**512.8**	696.0	608.8

Society **Value of collateral held**	Indexed 2017 £m	Unindexed 2017 £m	Indexed 2016 £m	Unindexed 2016 £m
Not impaired	**86.6**	**71.5**	84.8	71.5

The collateral held consists of properties, land or other guarantees or cash included within the above categories. The use of such collateral is in line with terms that are usual and customary to standard lending activities.

Forbearance strategies and renegotiated loans

Certain forbearance activities are applied on a small number of commercial mortgages. Loans that have been restructured (generally via a term extension) and would otherwise have been past due or impaired are classified as renegotiated. The carrying amount of loans that have been classified as renegotiated retain this classification until maturity or derecognition. Interest is recorded on renegotiated loans on the basis of new contractual terms following renegotiation.

The analysis below sets out the commercial mortgage balances with evidence of forbearance and renegotiated terms at the year end date.

Group	Arrangements 2017 £m	Capitalisation 2017 £m	Term extensions 2017 £m	Total 2017 £m
Loans neither past due or impaired	7.0	-	44.7	**51.7**
Not past due but impaired	-	11.2	10.9	**22.1**
Impaired				
Past due 6 to 12 months	13.0	-	-	**13.0**
Past due over 12 months	3.0	-	-	**3.0**
	23.0	**11.2**	**55.6**	**89.8**

Group	Arrangements 2016 £m	Capitalisation 2016 £m	Term extensions 2016 £m	Total 2016 £m
Loans neither past due or impaired	0.5	-	67.6	68.1
Not past due but impaired	4.6	11.3	20.6	36.5
Impaired				
Past due over 12 months	19.4	-	-	19.4
	24.5	11.3	88.2	124.0

32. Credit risk (continued)

Credit risk - loans and advances to credit institutions and investment securities

The Group holds treasury investments in order to meet liquidity requirements and for general business purposes. The credit risk arising from these investments is monitored, managed and controlled closely by the Group.

The Group determines that a treasury asset is impaired when there has been a significant or prolonged decline in the fair value below its cost. The determination of 'significant or prolonged' requires judgement. In making this judgement, the Group evaluates, among other factors, the normal volatility in valuation, evidence of deterioration in the financial health of the investee, industry and sector performance and operational and financing cash flows. At 31 March 2017 and 31 March 2016 none of the Group's treasury investments were either past due or impaired and no impairment charges were required during the year.

At 31 March 2017, 100.0% (2015/16: 100.0%) of the Group's treasury assets were invested in or deposited with counterparties rated single A or better or classified as a Global Systemically Important Counterparty (GSIC). The Group has no exposure in its liquidity portfolio to Greece, Ireland, Italy, Portugal or Spain, the emerging markets or to any mortgage market other than the UK. The tables below show the relative concentrations of the Group's treasury investment portfolio, all of which are denominated in sterling:

	Group 2017 £m	Group 2016 £m	**Society 2017 £m**	Society 2016 £m
Concentration by credit grading				
AAA	**344.2**	286.9	**344.2**	286.9
AA+ to AA-	**412.0**	353.9	**367.8**	295.6
A+ to A-	**76.1**	166.1	**38.0**	113.7
BBB+	**21.5**	21.6	**21.5**	21.6
Building societies	**-**	1.0	**-**	1.0
Other	**-**	-	**810.5**	889.8
	853.8	829.5	**1,582.0**	1,608.6
Concentration by sector				
Financial institutions	**219.9**	327.2	**137.5**	216.4
Asset backed securities	**249.4**	233.4	**1,060.0**	1,123.3
Supranational institutions	**89.7**	53.5	**89.7**	53.5
Sovereign	**294.8**	215.4	**294.8**	215.4
	853.8	829.5	**1,582.0**	1,608.6
Concentration by region				
UK	**669.8**	626.6	**1,458.5**	1,475.1
Europe (excluding UK)	**72.5**	86.3	**12.0**	16.9
North America	**7.2**	32.9	**7.2**	32.9
Australasia	**13.2**	28.8	**13.2**	28.8
Supranational	**89.7**	53.5	**89.7**	53.5
Asia	**1.4**	1.4	**1.4**	1.4
	853.8	829.5	**1,582.0**	1,608.6

33. Market risk

Market risk is the potential adverse change in Group income, or the value of Group net worth, arising from movements in interest rates, exchange rates, equity prices or other market prices. The Board recognises that the effective management of market risk is essential to the maintenance of stable earnings and the preservation of member value.

The Group's exposure to market risk is governed by the Board approved Treasury and Financial Risks Management Policy, which sets out the nature of risks that may be taken and defines aggregate risk limits. Within this Policy, the Board has delegated responsibility for the management and control of market rate risk to the Assets & Liabilities Committee (ALCo). At each meeting, ALCo reviews reports which show the Group's current and forecast exposure to market risks together with the results of extensive stress testing.

The Society's Assets and Liabilities Management function is responsible for operational management of the Group's exposure to market risk. It achieves this by taking advantage of natural hedges arising within the Group's businesses and, for the purpose of reducing risk, transacting appropriate hedging instruments where no natural hedges exist.

Interest rate risk

The Group's exposure to interest rate risk is reported against target operating ranges set by ALCo, which themselves fall within Board Policy limits. The effect upon the Group's current and forecast net market value of assets and liabilities is determined for parallel yield curve shifts in the range +2% to -2%, subject to a floor at 0%, and for a variety of stressed non-parallel yield curve shifts, including extreme convergent and divergent Bank Rate and LIBOR paths. The impact upon net interest income is also assessed for rate movements using the same parallel and non-parallel stress rates, including convergent and divergent Bank Rate and LIBOR paths.

Analysis is also presented to show the mismatches between assets and liabilities whose rates move in line with different variable rate benchmarks such as Bank Rate, LIBOR and rates administered by the Group. Such mismatches generate additional interest rate risks (basis risk) to those assessed by parallel and non-parallel shift analysis. The Board has imposed limits upon these absolute basis mismatches.

To ensure that the overall reported interest rate risk position does not mask excessive offsetting concentrations in different periods, reprice gap concentration limits are in place to limit the maximum mismatch between assets and liabilities repricing in any one month. In conducting this analysis, general reserves, PPDS and PIBS are allocated over a range of time buckets against treasury and other assets in accordance with targets set by ALCo. The resulting 'reverse cumulative gap report' allows the income and market value sensitivity of a one basis point movement in interest rates upon the whole balance sheet to be calculated.

The Group's gap and basis mismatch positions are reported quarterly to the Prudential Regulation Authority (PRA). The levels of Group pre-tax interest rate risk exposures to a 2% parallel shift, through the reporting period were as follows:

	At 31 March 2017 £m	Average 2017 £m	High 2017 £m	Low 2017 £m
Market value	**(2.1)**	(0.9)	(2.1)	0.2
Net interest income	**(0.5)**	(0.6)	(1.2)	(0.3)

Equity risk

Equity risk arises from index linked savings products offered by the Group and is managed through the use of derivative contracts. The Group's only exposure to equity risk at 31 March 2017 was £13.4m (2015/16: £47.9m) of fully hedged savings products.

Derivative financial instruments

Instruments used for risk management purposes include derivative financial instruments (derivatives). Derivatives are instruments whose value is derived from one or more underlying price, rate or index (such as interest rates, exchange rates or stock market indices) but have a smaller or no initial net investment relative to financial assets/liabilities offering the same risk/return, as cash flows are generally settled at a future date.

The Group uses derivatives to reduce market risk in its daily activities. Derivatives are not used in trading activity or for speculative purposes. The nature of these instruments means that the nominal value of these transactions is not included in the Statements of Financial Position. The interest payments, receipts and changes in fair value of derivatives and hedged items are recognised in the Income Statement. Fair values are recorded in the Statements of Financial Position.

Types of derivatives

The principal derivatives used by the Group are interest rate swaps and index linked swaps that are used to hedge Group Statement of Financial Position exposures.

The following table describes the significant activities undertaken by the Group, the related risks associated with such activities and the type of derivatives which are typically used in managing such risks. Such risks may also be managed using Statement of Financial Position instruments as part of an integrated approach to risk management.

Activity	Risk	Managed by
Management of the investment of reserves and other non-interest bearing liabilities	Sensitivity to changes in interest rates	Matching against fixed rate assets
Fixed rate mortgage lending and other assets	Sensitivity to rises in interest rates	Pay fixed rate interest rate swaps, matching against fixed rate liabilities
Fixed rate savings products and funding	Sensitivity to falls in interest rates	Receive fixed rate interest rate swaps, matching against fixed rate receipts
Equity linked investment products	Sensitivity to changes in equity indices	Equity linked swaps and options
Capped, collared or floored products	Sensitivity to changes in interest rates	Matching against appropriate cap, collar or floor derivatives or suitable assets or liabilities

34. Liquidity risk

The Society's principal purpose is to make loans secured by way of mortgage on residential property funded substantially by short-term savings from its members.

The contractual maturity of the mortgages is typically up to 25 years although loans are often repaid early due to borrowers moving house or remortgaging. In contrast, the majority of members' savings are available on demand or at short notice. It is this inherent mismatch between the maturity profile of mortgage lending and the easy accessibility of savings that creates liquidity risk.

The Group's exposure to liquidity risk is governed by the Liquidity and Funding Policy sections of the Board approved Treasury and Financial Risks Management Policy.

The Liquidity and Funding Policy limit framework is designed to ensure that adequate liquid assets are held to cover statutory, regulatory and operational cash requirements in both business-as-usual and stressed environments.

The Group's liquidity risk is managed as follows:

- The Board has delegated authority for the management of liquidity risk to the Assets & Liabilities Committee (ALCo) within risk tolerances set out in the Liquidity and Funding Policies. ALCo meets monthly;
- Operational management of liquidity risk is further delegated to the Liquidity Management Committee (LMC). LMC meets weekly to agree, based upon detailed customer behavioural analysis, the amount of funding required to maintain the adequacy of Group liquidity over horizons of up to three months. LMC plans cash requirements at a higher level over an extended rolling 12 month plan period;
- LMC also considers a series of daily, weekly and monthly stress tests which are designed to ensure that the Group maintains sufficient liquidity to meet its cash flow needs under any one of a number of adverse scenarios. These scenarios simulate both Group specific, general market and combined events including severe savings outflows and the unavailability of wholesale funding; and
- Under the Prudential Regulation Authority's liquidity regime, the Group is required to hold sufficient high quality liquid assets (buffer liquidity), such as government securities, supranational bonds, covered bonds and cash deposited with the Bank of England, to ensure that it can meet its liabilities over a 30 day period under stressed conditions. This is known as its Liquidity Coverage Ratio (LCR). The Group holds both buffer and other high quality liquidity above that required by the LCR in accordance with its own day-to-day assessment of liquidity adequacy.

There are three measures that the Group considers key to monitoring its liquidity position:

- Liquidity ratios - assesses daily the amount of buffer liquidity necessary to meet its LCR, and to maintain overall liquidity adequacy;
- Liquidity stress tests - models the adequacy of Group liquidity under a number of different stress scenarios within the context of the Board's liquidity risk tolerance; and
- Refinancing gaps - sets the maximum level of wholesale and combined retail/wholesale funding permitted to mature over given time periods.

Further details of liquidity management are contained within the Risk Management Report on pages 23 to 27.

The table below analyses the Group's assets and liabilities across maturity periods that reflect the residual maturity from the year end date to the contractual maturity date. The actual repayment profile of loans and advances is likely to be significantly different to that shown in the analysis.

At 31 March 2017

Group	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	287.6	-	-	-	-	7.2	**294.8**
Loans and advances to credit institutions	52.1	121.9	-	-	-	-	**174.0**
Investment securities	-	13.7	152.1	219.2	-	-	**385.0**
Derivative financial instruments	-	2.2	0.1	2.5	1.5	-	**6.3**
Loans and advances to customers	-	284.9	73.9	319.2	4,098.5	-	**4,776.5**
Deferred tax assets	-	-	-	-	-	16.4	**16.4**
Trade and other receivables	-	-	-	-	-	3.5	**3.5**
Intangible assets	-	-	-	-	-	13.3	**13.3**
Investment properties	-	-	-	-	-	128.9	**128.9**
Property, plant and equipment	-	-	-	-	-	32.1	**32.1**
	339.7	**422.7**	**226.1**	**540.9**	**4,100.0**	**201.4**	**5,830.8**
Liabilities and equity							
Shares	3,150.6	123.6	179.5	973.6	-	-	**4,427.3**
Amounts due to credit institutions	-	135.7	90.5	224.1	-	-	**450.3**
Amounts due to other customers	7.3	74.9	49.5	1.0	-	-	**132.7**
Derivative financial instruments	-	0.1	3.4	16.8	48.7	-	**69.0**
Debt securities in issue	-	58.0	-	145.7	59.5	-	**263.2**
Deferred tax liabilities	-	-	-	-	-	5.0	**5.0**
Trade and other payables	-	-	-	-	-	10.2	**10.2**
Provisions for liabilities	-	-	-	-	-	3.1	**3.1**
Retirement benefit obligations	-	-	-	-	-	6.5	**6.5**
Profit participating deferred shares	-	-	-	-	-	173.0	**173.0**
Subscribed capital	-	-	-	-	-	75.0	**75.0**
General reserves	-	-	-	-	-	211.0	**211.0**
Revaluation reserve	-	-	-	-	-	3.5	**3.5**
Available for sale reserve	-	-	-	-	-	1.7	**1.7**
Cash flow hedging reserve	-	-	-	-	-	(0.7)	**(0.7)**
	3,157.9	**392.3**	**322.9**	**1,361.2**	**108.2**	**488.3**	**5,830.8**

34. Liquidity risk (continued)

At 31 March 2016

Group	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	208.7	-	-	-	-	6.7	215.4
Loans and advances to credit institutions	80.4	123.6	-	-	-	-	204.0
Investment securities	-	56.1	92.1	261.9	-	-	410.1
Derivative financial instruments	-	1.5	3.0	3.8	0.6	-	8.9
Loans and advances to customers	-	333.6	98.1	309.1	3,998.2	-	4,739.0
Deferred tax assets	-	-	-	-	-	20.4	20.4
Trade and other receivables	-	-	-	-	-	2.7	2.7
Intangible assets	-	-	-	-	-	8.2	8.2
Investment properties	-	-	-	-	-	123.7	123.7
Property, plant and equipment	-	-	-	-	-	33.9	33.9
Retirement benefit assets	-	-	-	-	-	0.8	0.8
	289.1	514.8	193.2	574.8	3,998.8	196.4	5,767.1
Liabilities and equity							
Shares	3,355.2	182.1	208.7	639.1	-	-	4,385.1
Amounts due to credit institutions	-	54.2	134.6	70.2	-	-	259.0
Amounts due to other customers	8.6	84.2	64.2	-	-	-	157.0
Derivative financial instruments	-	0.3	3.0	23.5	50.3	-	77.1
Debt securities in issue	-	-	-	296.0	72.6	-	368.6
Deferred tax liabilities	-	-	-	-	-	4.7	4.7
Trade and other payables	-	-	-	-	-	15.2	15.2
Provisions for liabilities	-	-	-	-	-	2.7	2.7
Profit participating deferred shares	-	-	-	-	-	179.5	179.5
Subscribed capital	-	-	-	-	-	74.9	74.9
General reserves	-	-	-	-	-	239.3	239.3
Revaluation reserve	-	-	-	-	-	3.4	3.4
Available for sale reserve	-	-	-	-	-	0.9	0.9
Cash flow hedging reserve	-	-	-	-	-	(0.3)	(0.3)
	3,363.8	320.8	410.5	1,028.8	122.9	520.3	5,767.1

At 31 March 2017

Society	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	287.6	-	-	-	-	7.2	**294.8**
Loans and advances to credit institutions	9.0	82.7	-	-	-	-	**91.7**
Investment securities	-	66.4	152.1	259.8	717.2	-	**1,195.5**
Derivative financial instruments	-	2.2	0.1	2.5	1.4	-	**6.2**
Loans and advances to customers	-	10.6	16.5	114.8	2,521.8	-	**2,663.7**
Deferred tax assets	-	-	-	-	-	11.7	**11.7**
Trade and other receivables	-	-	-	-	-	3.3	**3.3**
Investments	-	-	-	-	-	1,526.9	**1,526.9**
Intangible assets	-	-	-	-	-	12.7	**12.7**
Property, plant and equipment	-	-	-	-	-	32.1	**32.1**
	296.6	**161.9**	**168.7**	**377.1**	**3,240.4**	**1,593.9**	**5,838.6**
Liabilities and equity							
Shares	3,150.6	123.6	179.5	973.6	-	-	**4,427.3**
Amounts due to credit institutions	-	135.7	90.5	224.1	-	-	**450.3**
Amounts due to other customers	8.5	78.1	56.2	37.6	209.9	-	**390.3**
Derivative financial instruments	-	0.1	3.4	16.5	39.7	-	**59.7**
Deferred tax liabilities	-	-	-	-	-	1.0	**1.0**
Trade and other payables	-	-	-	-	-	9.4	**9.4**
Provisions for liabilities	-	-	-	-	-	3.0	**3.0**
Retirement benefit obligations	-	-	-	-	-	6.5	**6.5**
Profit participating deferred shares	-	-	-	-	-	173.0	**173.0**
Subscribed capital	-	-	-	-	-	75.0	**75.0**
General reserves	-	-	-	-	-	237.9	**237.9**
Revaluation reserve	-	-	-	-	-	3.5	**3.5**
Available for sale reserve	-	-	-	-	-	1.7	**1.7**
	3,159.1	**337.5**	**329.6**	**1,251.8**	**249.6**	**511.0**	**5,838.6**

34. Liquidity risk (continued)

At 31 March 2016

Society	Repayable on demand £m	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	No specific maturity £m	Total £m
Assets							
Cash and balances with the Bank of England	208.7	-	-	-	-	6.7	215.4
Loans and advances to credit institutions	11.7	81.5	-	-	-	-	93.2
Investment securities	-	56.1	92.1	355.2	796.6	-	1,300.0
Derivative financial instruments	-	1.5	3.0	3.8	0.5	-	8.8
Loans and advances to customers	-	14.8	13.4	104.9	2,247.0	-	2,380.1
Deferred tax assets	-	-	-	-	-	13.5	13.5
Trade and other receivables	-	-	-	-	-	2.7	2.7
Investments	-	-	-	-	-	1,669.2	1,669.2
Intangible assets	-	-	-	-	-	7.6	7.6
Property, plant and equipment	-	-	-	-	-	33.9	33.9
Retirement benefit assets	-	-	-	-	-	0.8	0.8
	220.4	153.9	108.5	463.9	3,044.1	1,734.4	5,725.2
Liabilities and equity							
Shares	3,355.2	182.1	208.7	639.1	-	-	4,385.1
Amounts due to credit institutions	-	54.2	134.6	70.2	-	-	259.0
Amounts due to other customers	10.4	88.0	68.3	45.3	288.0	-	500.0
Derivative financial instruments	-	0.3	3.0	23.1	41.0	-	67.4
Deferred tax liabilities	-	-	-	-	-	0.6	0.6
Trade and other payables	-	-	-	-	-	14.2	14.2
Provisions for liabilities	-	-	-	-	-	2.6	2.6
Profit participating deferred shares	-	-	-	-	-	179.5	179.5
Subscribed capital	-	-	-	-	-	74.9	74.9
General reserves	-	-	-	-	-	237.6	237.6
Revaluation reserve	-	-	-	-	-	3.4	3.4
Available for sale reserve	-	-	-	-	-	0.9	0.9
	3,365.6	324.6	414.6	777.7	329.0	513.7	5,725.2

The significant development of liquidity stress testing and forecast models has continued throughout 2017 due to economic and market conditions. A wide range of scenarios is considered including mild and severe stresses, credit downgrades and a total closure of the wholesale market. An analysis of the liquidity portfolio is set out in the table below:

Group	2017 £m	2017 %	2016 £m	2016 %
Cash in hand and balances with the Bank of England	**294.8**	**34.5**	215.4	26.0
Cash with banks and building societies	**174.0**	**20.4**	204.0	24.6
Fixed rate bonds	**65.3**	**7.7**	42.9	5.2
Floating rate notes	**70.3**	**8.2**	135.1	16.3
Covered bonds	**137.8**	**16.1**	124.0	14.9
Residential mortgage backed securities	**111.6**	**13.1**	108.1	13.0
Total	**853.8**	**100.0**	829.5	100.0

During the year the liquidity balances have increased from £829.5m at 31 March 2016 to £853.8m at 31 March 2017. Expressed as a proportion of combined shares and deposits liabilities, this represents a decrease from 17.28% to 17.04%.

The following table is an analysis of the gross contractual cash flows payable under financial liabilities:

At 31 March 2017

Group	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	4,011.1	185.8	266.5	-	**4,463.4**
Amounts due to credit institutions and other customers	202.0	141.2	227.3	74.9	**645.4**
Debt securities in issue	58.3	2.0	153.0	104.6	**317.9**
Derivative financial instruments	3.7	13.6	45.3	25.0	**87.6**
	4,275.1	**342.6**	**692.1**	**204.5**	**5,514.3**

At 31 March 2016

Group	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	3,815.8	345.8	251.2	-	4,412.8
Amounts due to credit institutions and other customers	146.8	179.4	72.0	74.9	473.1
Debt securities in issue	1.5	4.0	302.9	118.2	426.6
Derivative financial instruments	7.4	21.0	77.5	86.0	191.9
	3,971.5	550.2	703.6	279.1	5,504.4

34. Liquidity risk (continued)

At 31 March 2017

Society	**Less than 3 months £m**	**3 to 12 months £m**	**1 to 5 years £m**	**Over 5 years £m**	**Total £m**
Liabilities					
Shares	4,011.1	185.8	266.5	-	**4,463.4**
Amounts due to credit institutions and other customers	202.0	141.2	227.3	74.9	**645.4**
Derivative financial instruments	3.2	12.6	40.7	21.2	**77.7**
	4,216.3	**339.6**	**534.5**	**96.1**	**5,186.5**

At 31 March 2016

Society	Less than 3 months £m	3 to 12 months £m	1 to 5 years £m	Over 5 years £m	Total £m
Liabilities					
Shares	3,815.8	345.8	251.2	-	4,412.8
Amounts due to credit institutions and other customers	146.8	179.4	72.0	74.9	473.1
Derivative financial instruments	6.3	17.9	60.6	1.8	86.6
	3,968.9	543.1	383.8	76.7	4,972.5

For each material class of financial liability a maturity analysis is provided on pages 99 to 102.

35. Financial commitments

	Group 2017 £m	Group 2016 £m	Society 2017 £m	Society 2016 £m
a) Capital commitments				
Capital expenditure contracted but not yet provided for in the accounts	**0.3**	4.2	**0.3**	4.2
b) Leasing commitments				
Total commitments under non-cancellable leases				
Rental commitments arising:				
Within one year	**0.5**	0.4	**0.5**	0.4
Later than one year and not later than five years	**1.5**	0.9	**1.5**	0.9
After five years	**-**	0.2	**-**	0.2
	2.0	1.5	**2.0**	1.5
c) Loan commitments				
Undrawn loan facilities	**144.0**	159.4	**144.0**	159.4

36. Related party transactions

i) Subsidiary, parent and ultimate controlling party

The Group is controlled by West Bromwich Building Society which is considered to be the ultimate parent undertaking. The subsidiaries of the Society are detailed in note 15. The Group's registered office and principal place of business is 2 Providence Place, West Bromwich, B70 8AF.

ii) Key management personnel

The Board considers key management personnel to comprise Executive and Non-Executive Directors. Details of Directors' emoluments are disclosed in note 8.

iii) Transactions with key management personnel and their close family members

The table below shows outstanding balances and transactions with key management personnel, which comprises Group Directors, and their close family members:

Group and Society	No. of key management personnel 2017	Amount in respect of key management personnel and their close family members 2017 £000	No. of key management personnel 2016	Amount in respect of key management personnel and their close family members 2016 £000
Savings balances at 31 March	**10**	**59**	9	17
Interest payable on savings balances	**10**	**-**	9	-

Mortgage loans and savings are available to key management personnel and members of their close family at normal commercial terms. At 31 March 2017, there were no mortgage loans (2015/16: nil) outstanding to Directors and their connected persons.

A register is maintained by the Society containing details of loans and transactions and arrangements made between the Society or its subsidiary undertakings and Directors of the Society or persons connected with Directors of the Society. The register will be available for inspection by members at the Annual General Meeting and during normal office hours at the Society's Principal Office (2 Providence Place, West Bromwich) during the period 15 days prior to the meeting.

iv) Contributions to pension schemes

During the year the Group paid contributions of £3.4m (2015/16: £9.5m) to defined benefit pension schemes, which are classified as related parties.

As part of the ongoing funding agreement for the West Bromwich Building Society Staff Retirement Scheme (the SRS), the Trustees of the SRS have been granted a charge over the Society's Head Office, which may be exercised only in the event of the Society defaulting on its pension obligations and in such circumstances assigns the rights of ownership of the building to the SRS.

36. Related party transactions (continued)

v) Transactions with Group companies

	Interest paid to Society 2017 £m	Interest paid to Society 2016 £m
Insignia Finance Limited	**0.3**	0.4
West Bromwich Commercial Limited	**17.6**	20.6
West Bromwich Homes Limited	**2.9**	2.9
West Bromwich Mortgage Company Limited	**21.4**	32.8
	42.2	56.7

At the year end the following balances were outstanding with Group companies:

	Loans owed by subsidiaries 2017 £m	Loans owed by subsidiaries 2016 £m
Insignia Finance Limited	**7.3**	12.2
Kenrick No. 1 Plc	**-**	0.2
West Bromwich Commercial Limited	**489.8**	586.1
West Bromwich Homes Limited	**122.1**	86.4
West Bromwich Mortgage Company Limited	**907.1**	983.7
	1,526.3	1,668.6

Transactions and balances between Group companies are on normal commercial terms and conditions.
The loans owed by West Bromwich Commercial Limited are net of impairment provisions of £78.2m (2015/16: £40.7m).

37. Business segments

Operating segments are reported in accordance with the internal reporting provided to the Group Board (the chief operating decision maker), which is responsible for allocating resources to the reportable segments and assessing their performance.

The Group has three main business segments:

- Retail - incorporating residential lending, savings, investments and protection;
- Commercial - primarily representing loans for commercial property investment; and
- Property - a portfolio of residential properties for rent.

Central Group operations have been included in Retail and comprise risk management, finance, treasury services, human resources and computer services, none of which constitute a separately reportable segment.

There were no changes to reportable segments during the year.

Transactions between the business segments are carried out at arm's length. The revenue from external parties reported to the Group Board is measured in a manner consistent with that in the consolidated Income Statement.

Funds are ordinarily allocated between segments, resulting in funding cost transfers disclosed in inter-segment net interest income. Interest charged for these funds is based on the Group's cost of capital. Central administrative costs are also allocated between segments and are disclosed in inter-segment administrative expenses. There are no other material items of income or expense between the business segments.

The Group does not consider its operations to be cyclical or seasonal in nature.

Income Statements for the year ended 31 March 2017

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Interest receivable and similar income	107.2	18.2	-	(16.5)	**108.9**
Interest expense and similar charges	(52.4)	(14.8)	(2.9)	16.5	**(53.6)**
Net interest receivable/(expense)	**54.8**	**3.4**	**(2.9)**	**-**	**55.3**
Fees and commissions receivable	2.7	-	-	-	**2.7**
Other operating income	37.5	-	4.1	(37.5)	**4.1**
Total operating income	**95.0**	**3.4**	**1.2**	**(37.5)**	**62.1**
Fair value (losses)/gains on financial instruments	(0.3)	0.1	-	-	**(0.2)**
Net realised gains	0.5	-	-	-	**0.5**
Total income	**95.2**	**3.5**	**1.2**	**(37.5)**	**62.4**
Administrative expenses	(42.5)	(1.7)	(0.2)	-	**(44.4)**
Depreciation and amortisation	(5.7)	-	-	-	**(5.7)**
Operating profit before revaluation gains, impairment and provisions	**47.0**	**1.8**	**1.0**	**(37.5)**	**12.3**
Gains on investment properties	-	-	5.4	-	**5.4**
Impairment on loans and advances	3.5	(11.1)	-	-	**(7.6)**
Provisions for liabilities	(67.4)	-	-	37.5	**(29.9)**
(Loss)/Profit before tax	**(16.9)**	**(9.3)**	**6.4**	**-**	**(19.8)**

Statements of Financial Position at 31 March 2017

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Total assets	**5,744.3**	**548.8**	**132.1**	**(594.4)**	**5,830.8**
Total liabilities	**5,295.2**	**588.6**	**125.8**	**(642.3)**	**5,367.3**
Capital expenditure	**9.0**	**-**	**-**	**-**	**9.0**

37. Business segments (continued)

Income Statements for the year ended 31 March 2016

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Interest receivable and similar income	123.2	19.4	-	(15.9)	126.7
Interest expense and similar charges	(65.0)	(14.7)	(2.9)	15.9	(66.7)
Net interest receivable/(expense)	58.2	4.7	(2.9)	-	60.0
Fees and commissions receivable	3.7	-	-	-	3.7
Other operating income	30.5	-	4.1	(30.7)	3.9
Total operating income	92.4	4.7	1.2	(30.7)	67.6
Fair value (losses)/gains on financial instruments	(1.2)	0.6	-	(0.4)	(1.0)
Net realised gains	0.6	-	-	-	0.6
Total income	91.8	5.3	1.2	(31.1)	67.2
Administrative expenses	(40.1)	(1.7)	(0.2)	-	(42.0)
Depreciation and amortisation	(5.1)	-	-	-	(5.1)
Operating profit before revaluation gains, impairment and provisions	46.6	3.6	1.0	(31.1)	20.1
Gains on investment properties	-	-	5.5	-	5.5
Impairment on loans and advances	(0.2)	(7.9)	-	-	(8.1)
Provisions for liabilities	(34.8)	-	-	30.8	(4.0)
Profit/(Loss) before tax	11.6	(4.3)	6.5	(0.3)	13.5

Statements of Financial Position at 31 March 2016*

	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
Total assets	5,656.6	643.2	128.1	(660.8)	5,767.1
Total liabilities	5,183.1	662.2	90.3	(666.2)	5,269.4
Capital expenditure	10.0	-	-	-	10.0

* Prior year comparatives have been restated to remove intra-divisional netting with a matching movement in consolidation adjustments.

38. Asset encumbrance

Certain financial assets have been utilised as collateral to support the wholesale funding initiatives of the Group. As the Group has retained substantially all of the risks and rewards of ownership, the assets remain on the Statement of Financial Position but are encumbered and cannot be utilised for other purposes.

As described in note 13, the Group has established a number of securitisation structures funded by the issue of mortgage backed securities (MBSs). Retained MBSs and designated mortgage loan pools may be pledged as collateral for participation in Bank of England funding schemes.

For liquidity management purposes, the Society also enters into sale and repurchase agreements whereby it sells investment securities to third parties with a commitment to repurchase them at a future date. The proceeds of the sale and repurchase agreements are included within amounts due to credit institutions.

An analysis of Group assets pledged at 31 March is set out below.

	Encumbered 2017 £m	**Unencumbered 2017 £m**	Encumbered 2016 £m	Unencumbered 2016 £m
Cash and balances at the Bank of England	**-**	**294.8**	-	215.4
Loans and advances to credit institutions	**59.5**	**114.5**	30.1	173.9
Investment securities	**10.0**	**375.0**	-	410.1
Derivative financial instruments	**-**	**6.3**	-	8.9
Loans and advances to customers	**1,134.9**	**3,641.6**	1,009.1	3,729.9
Other assets	**-**	**194.2**	-	189.7
	1,204.4	**4,626.4**	1,039.2	4,727.9

In addition to the above, at 31 March 2017, Group loans and advances to credit institutions included £82.6m (2015/16: £81.5m) of collateral pledged against derivative financial instruments and £1.4m (2015/16: £1.4m) cash collateral paid in relation to sale and repurchase agreements.

39. Country-by-country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 introduced reporting obligations for institutions within the scope of the European Union's Capital Requirements Directive (CRD IV). The requirements aim to give increased transparency regarding the activities of institutions.

West Bromwich Building Society (the Society) is the 7th largest building society in the UK. As a mutual organisation, the Society is owned and run for the benefit of its members with the safety of members' funds being paramount. In providing a safe haven for members' funds, the Society can fulfil its primary purpose of enabling home ownership through the provision of mortgages.

These consolidated financial statements of the West Bromwich Building Society Group (the Group) include the audited results of the Society, its subsidiary undertakings and a number of securitisation entities. The consolidated entities, their principal activities and countries of incorporation are detailed in note 15. All of the consolidated entities are incorporated in the United Kingdom (UK), with the exception of Hawthorn Finance Limited which is incorporated in Jersey.

Basis of preparation

- The number of employees has been calculated as the average number of full and part-time employees, on a monthly basis, as disclosed in note 7.
- Turnover represents Group total income as disclosed in the Group Income Statement. Total income comprises net interest, fees and commissions receivable and other operating income, together with fair value gains/losses and net realised profits/losses on financial instruments.
- Pre-tax profit or loss represents the Group profit or loss before tax, as reported in the Group Income Statement.
- Corporation tax paid represents the amount of tax paid during the year, as disclosed in the Group Cash Flow Statement.
- Public subsidies received represent direct support by the government and exclude any central bank operations that are designed for financial stability purposes or operations that aim to facilitate the functioning of the monetary policy transmission mechanism.

For the year ended 31 March 2017:

- Hawthorn Finance Limited did not transact with entities outside the Group and had no employees (2015/16: nil).
- Group total income, all of which arose in the UK, was £62.4m (2015/16: £67.2m).
- Group loss before tax, all of which arose in the UK, was £19.8m (2015/16: profit of £13.5m).
- The average number of Group employees, all of which were employed in the UK, was 758 (2015/16: 740).
- The Group made corporation tax payments of £nil (2015/16: £nil) in the UK.
- The Group received no public subsidies (2015/16: £nil).

Annual Business Statement

1. Statutory percentages

	2017 %	Statutory limit %
Lending limit	**11.5**	25.0
Funding limit	**11.7**	50.0

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 secured on residential property. Business assets are the total assets of the Group plus allowance for losses on loans and advances less liquid assets, investment properties, intangible assets and property, plant and equipment as shown in the Group Statement of Financial Position.

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

Securitised assets and related liabilities are excluded from the lending limit and funding limit calculations in line with the Building Societies Act 1986 as updated by the Modification of the Lending Limit and Funding Limit Calculations Order 2004.

The statutory limits are as laid down under the Building Societies Act 1986 as amended by the Building Societies Act 1997 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 its members.

2. Other percentages

	2017 %	2016 %
As a percentage of shares and borrowings:		
Gross capital	**9.25**	10.37
Free capital	**6.21**	7.29
Liquid assets	**17.04**	17.28
As a percentage of mean total assets:		
(Loss)/Profit for the financial year	**(0.44)**	0.17
Management expenses	**0.86**	0.83

The above percentages have been prepared from the Group's accounts and in particular:

- 'Shares and borrowings' represent the total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue excluding non-recourse finance, in each case including accrued interest.
- 'Gross capital' represents the aggregate of general reserves, available for sale reserve, revaluation reserve, cash flow hedging reserve, subscribed capital and profit participating deferred shares.
- 'Free capital' represents the aggregate of gross capital and collective impairment provisions for losses on loans and advances less intangible assets, investment properties and property, plant and equipment.
- 'Mean total assets' represent the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.
- 'Liquid assets' represent the total of cash and balances with the Bank of England, loans and advances to credit institutions and investment securities.
- 'Management expenses' represent the aggregate of administrative expenses, depreciation and amortisation.

Information relating to Directors' and Officers' other directorships and interests at 31 March 2017

Name, qualification and age	Role	Date of appointment	Other directorships and interests
Claire Hafner MA, ACA Age 57	Non-Executive Director	1 September 2011	Monecor (London) Limited 9 Winthorpe Road Freehold Limited ATM UK Limited Glendrake Limited Franklin UK Midco Limited Franklin Ireland Topco Limited Fintrax Group Holdings Limited Fintrax Payment Systems GmbH (Austria) Fintrax Italy S.R.L. (Italy) Premier Tax Free ehf (Iceland) Premier Tax Free S.R.L. (Italy) Premier Tax Free & Fintrax Payments (Asia) PTE. Ltd (Singapore) Premier Tax Free (Malta) Limited
Julie Hopes MBA, ACIB Age 49	Non-Executive Director	1 April 2016	Police Mutual Assurance Society Co-op General Insurance
Mark Nicholls MA (Cantab), MBA Age 68	Chairman	1 January 2010	Northern Investors Company PLC Rathbone Brothers Plc Rathbone Investment Management Ltd
Mark Preston BA (Hons), ACIB Age 57	Non-Executive Director	18 May 2011	Monecor (London) Ltd
Martin Ritchley FCA, FCIB, Hon DBA (Coventry) Age 70	Deputy Chairman and Senior Independent Director	1 September 2009	Royal Shakespeare Theatre Trust
Richard Sommers MA (Oxon), ACIB Age 60	Non-Executive Director	1 October 2009	Sidmouth Rugby Football Club Limited
Colin Walklin BSc, FCA Age 63	Non-Executive Director	20 July 2011	Standard Life Employee Services Limited Standard Life Oversea Holdings Limited Standard Life Wealth Limited Standard Life Portfolio Investments Limited Standard Life Investments (Holdings) Limited Standard Life Investments Limited
Mark Gibbard BSc, FCA, MCT Age 55	Group Finance & Operations Director	16 February 2011	
Ashraf Piranie MBA, FCCA Age 53	Group Finance & Operations Director	13 March 2017	Elite Star Investments Limited Osborne House Property Management Limited DPC (2011) Limited West Bromwich Mortgage Company Limited CL Mortgages Limited
Jonathan Westhoff BA (Hons) Financial Services, FCMA, CGMA, ACIB Age 52	Chief Executive	5 May 2009	West Bromwich Commercial Limited West Bromwich Homes Limited West Bromwich Mortgage Company Limited CL Mortgages Limited

All Directors are members of the Society. None of the Directors have at any time in the year, or at the year end, any beneficial interest in shares or debentures of any associated body of the Society.

Service contracts

The Society's policy in relation to the duration of contracts for the Executive Directors is that their contract would normally continue until termination by either party, subject to the required notice or until retirement. The service contract is terminable with 12 months' notice if given by the Society or six months' notice if given by the Director. Jonathan Westhoff entered into his contract as Chief Executive on 25 May 2011 and Ashraf Piranie entered into his service contract on 13 March 2017, on this basis. Mark Gibbard retired from the Society on 31 March 2017 after giving the Society 12 months' notice.

For further details of the Executive Directors' service contracts, see the Directors' Remuneration Report on pages 40 to 46.

Documents may be served on any of the above named Directors at the following address: Addleshaw Goddard, 3 Sovereign Square, Sovereign Street, Leeds LS1 4ER.

Senior management	Role	Directorships and interests
Peter Collingridge BSc (Hons), MEng	Divisional Director, IT	
Manjit Hayre	Chief Financial Risk Officer	
Greg Johnson ACIB	Divisional Director, Change	
Thomas Lynch MA, ACA	Divisional Director, Treasury & Finance	Central Processing Limited CL Mortgages Limited White Label Lending Limited Sandwell Commercial Finance No. 1 Plc Sandwell Commercial Finance No. 2 Plc Sandwell Finance Holdings Limited West Bromwich Mortgage Company Limited
John McErlean MIIA, FIIA	Divisional Director, Internal Audit	
Neil Noakes	Group Secretary	Insignia Finance Limited West Bromwich Homes Limited White Label Lending Limited
Jacqui Randle BSc, FCIPD	Divisional Director, Human Resources	WBBS (SRS) Limited
Stephen Smart	Divisional Director, Operations	CL Mortgages Limited Insignia Finance Limited West Bromwich Commercial Limited West Bromwich Mortgage Company Limited White Label Lending Limited
James Wright BSc, ACIB, CIM Dip	Divisional Director, Sales & Marketing	Central Processing Limited CL Mortgages Limited West Bromwich Mortgage Company Limited

Glossary

Set out below are the definitions of the terms used within the Annual Report and Accounts to assist the reader and to facilitate comparison with other financial institutions:

Arrears – Customers are said to be in arrears when they are behind in fulfilling their obligations with the result that an outstanding loan commitment is unpaid or overdue. The value of the arrears is the value of the payments that have been missed.

Asset backed securities (ABS) – Securities that represent an interest in an underlying pool of referenced assets. Typically these assets are pools of residential or commercial mortgages.

Basel III – In December 2010, the Basel Committee on Banking Supervision issued the Basel III rules text, which presents the details of the strengthened global regulatory standards on bank capital adequacy and liquidity. The requirements, embedded using CRD IV, became effective from 1 January 2014.

Buffer liquidity – Cash and investments with the UK government (deposits with the Bank of England or holdings of UK Gilts and similar investments) and with supranational institutions. The limit is set by the Prudential Regulation Authority (PRA).

Capital Requirements Regulation and Capital Requirements Directive IV (CRD IV) – CRD IV is the legislative package made up of the Capital Requirements Regulation and the Capital Requirements Directive to implement the Basel III agreement.

Commercial lending – Loans secured on commercial assets. Commercial assets can include office buildings, industrial property, hotels, medical centres, shopping centres, farm land, buy to let and housing association properties.

Commercial mortgage backed securities (CMBS) – Securities that represent interests in a pool of commercial mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).

Common Equity Tier 1 capital (CET1) – CET1 capital comprises internally generated capital from general reserves and other reserves less intangible assets, goodwill and other regulatory adjustments.

Common Equity Tier 1 capital ratio – Common Equity Tier 1 capital as a percentage of risk weighted assets.

Contractual maturity – The final payment date of a loan or other financial instrument, at which point all the remaining outstanding principal and interest is due to be paid.

Credit risk – The risk that a customer or counterparty is unable to honour their obligations as they fall due.

Debt securities in issue – Transferable certificates of indebtedness of the Group to the bearer of the certificates. These are liabilities of the Group and include certificates of deposit and non-recourse finance.

Derivative financial instruments – A derivative financial instrument is a type of financial instrument (or an agreement between two parties) whose value depends on the underlying asset, index or reference rate it is linked to. The Group uses derivative financial instruments to hedge its exposures to market risks such as interest rate, equity and currency risk.

Effective interest method – The method used to measure the carrying value of a financial asset or a liability and to allocate associated interest income or expense over the relevant period. The calculation includes all fees and penalties paid or received between parties to the contract that are considered integral.

Fair value – Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

Financial Services Compensation Scheme (FSCS) – The UK's compensation fund of last resort for customers of authorised financial services firms. The FSCS may pay compensation to customers if a firm is unable, or likely to be unable, to pay claims against it, usually because it has stopped trading or has been declared in default. The FSCS is funded by the financial services industry. Every deposit taking firm authorised by the PRA is obliged to pay an annual levy, which goes towards its running costs and compensation payments.

Free capital – The aggregate of gross capital and collective impairment provisions for losses on loans and advances to customers less intangible assets, investment properties and property, plant and equipment.

Funding for Lending Scheme (FLS) – A scheme launched by the Bank of England and HM Treasury providing funding to incentivise banks and building societies to boost lending to the economy.

Funding limit – Measures the proportion of shares and borrowings not in the form of shares held by individuals excluding non-recourse finance. The calculation of the funding limit is explained in the Annual Business Statement.

Goodwill – Goodwill arises on the acquisition of subsidiary undertakings, joint ventures, associates or businesses and represents the excess of the fair value of consideration over the fair value of identifiable net assets and contingent liabilities acquired at the date of acquisition.

Gross capital – The aggregate of general reserves, available for sale reserve, revaluation reserve, cash flow hedging reserve, subscribed capital and profit participating deferred shares.

Impaired loans – Loans which have been assessed and there is evidence to suggest that the Group will not receive all of the contractual cash flows or there is an expectation that the cash flows will be received at a later date than when they are contractually due.

Individual Liquidity Adequacy Assessment (ILAA) – The Group's internal assessment of the levels of liquidity that need to be held by the Society to meet its regulatory liquidity requirements.

Individually/collectively assessed – At each Statement of Financial Position date the Group assesses whether or not there is objective evidence that individual financial assets are impaired. If no objective evidence of impairment exists for an individually assessed financial asset, it is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment. A collective provision is made against a group of financial assets where there is evidence that credit losses have been incurred, but not individually identified, at the reporting date.

Interest rate risk – Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market interest rates.

Internal Capital Adequacy Assessment Process (ICAAP) – The Group's own assessment, as part of regulatory requirements, of the levels of capital that it needs to hold in respect of the risks it faces under a business as usual scenario and a variety of stress scenarios.

International Swaps and Derivatives Association (ISDA) master agreement – A standardised contract developed by ISDA and used to enter into bilateral derivatives transactions.

Investment securities – Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings.

Lending limit – Measures the proportion of business assets not in the form of loans fully secured on residential property. The calculation of the lending limit is explained in the Annual Business Statement.

Leverage ratio – Tier 1 capital as a percentage of total exposures which include on and off balance sheet assets after netting derivatives.

Liquid assets – Total of cash in hand and balances with the Bank of England, loans and advances to credit institutions and investment securities.

Liquidity coverage ratio (LCR) – A Basel III measure to ensure sufficient highly liquid assets cover expected net cash outflows under a 30-day liquidity stress scenario.

Liquidity risk – The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash inflows and outflows.

Loan to value ratio (LTV) – A ratio which expresses the amount of a mortgage as a percentage of the value of the property on which it is secured. The Group calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI)).

Loans past due/past due loans – Loans on which payments are overdue including those on which partial payments are being made.

Management expenses – Management expenses represent administrative expenses. The management expense ratio is management expenses expressed as a percentage of mean total assets.

Market risk – The risk that movements in market risk factors, including foreign exchange rates, interest rates, credit spreads and customer-driven factors will reduce income or portfolio values.

Mean total assets – Represents the amount produced by halving the aggregate of total assets at the beginning and end of the financial year.

Medium term notes (MTN) – Securities offered by a company to investors, through a dealer, across a range of maturities.

Member – A person who has a share investment or a mortgage loan with the Society.

Mortgage backed securities (MBS) – Assets which are referenced to underlying mortgages.

Net interest income – The difference between interest received on assets and interest paid on liabilities.

Net interest margin – This ratio calculates the net interest income as a percentage of mean total assets.

Net stable funding ratio (NSFR) – A ratio calculated as the amount of available stable funding against the amount of required stable funding. This measure will be taken over an observation period of one year.

Non-recourse finance – A secured loan (debt) that is secured by a pledge of collateral but for which the borrower is not personally liable. If the borrower defaults, the lender can seize the collateral, but the lender's recovery is limited to the collateral alone.

Operational risk – The risk of loss arising from inadequate or failed internal processes, people and systems or from external events.

Other income – The income received from selling non-mortgage and savings products (e.g. home and contents insurance, investment products, other insurances and property rental income).

Permanent interest bearing shares (PIBS) – Unsecured, deferred shares that rank behind the claims of all depositors, payables and investing members of the West Brom and rank equally with profit participating deferred shares.

Prime – Prime mortgages are those granted to the most credit worthy category of borrower.

Profit participating deferred shares (PPDS) – A form of unsecured capital that are included as Common Equity Tier 1 capital. PPDS rank behind the claims of all depositors, payables and investing members of the West Brom and rank equally with PIBS.

Renegotiated loans – Loans are classed as renegotiated with the customer's consent, when their terms have changed during the year. Loans and advances are generally renegotiated either as part of an ongoing customer relationship or in response to an adverse change in the circumstances of the borrower.

Repo/Reverse repo – Short to medium-term funding agreements which allow a borrower to sell a financial asset, such as asset backed securities (ABS) or government bonds as security for cash. As part of the agreement the borrower agrees to repurchase the security at some later date. For the party selling the security (and agreeing to repurchase it in the future) it is a repo; for the party on the other end of the transaction (buying the security and agreeing to sell in the future), it is a reverse repurchase agreement or reverse repo.

Residential loans – Money loaned to individuals rather than institutions. Residential mortgage lending is secured against residential property.

Residential mortgage backed securities (RMBS) – A category of asset backed securities (ABS) that represents interests in a group of residential mortgages. Investors in these securities have the right to cash received from future mortgage payments (interest and/or principal).

Risk appetite – The articulation of the level of risk that the Group is willing to take (or not take) in order to safeguard the interests of the Society's members whilst achieving business objectives.

Risk weighted assets (RWA) – The value of assets, after adjustment, under Basel III rules to reflect the degree of risk they represent.

Securitisation – A process by which a group of assets, usually loans, are aggregated into a pool which is used to back the issuance of new securities. An entity transfers these assets to a structured entity which then issues securities backed by the assets. The Group has established securitisation structures as part of its funding activities.

Shares – Money deposited by a person in a retail savings account with the Society. Such funds are recorded as liabilities for the Society.

Shares and borrowings – The total of shares, amounts owed to credit institutions, amounts owed to other customers and debt securities in issue, including accrued interest and fair value adjustments for hedged risk.

Sub-prime – Loans to borrowers typically having weakened credit histories that include payment delinquencies and, in some cases, potentially more severe problems such as court judgements and discharged bankruptcies.

Term Funding Scheme (TFS) – A scheme launched by the Bank of England, providing term funding to banks and building societies with the aim of promoting UK lending growth.

Tier 1 capital – An element of regulatory capital and measure of financial strength, comprising Common Equity Tier 1 and Additional Tier 1 capital. Additional Tier 1 capital is not deemed to be fully loss absorbing and can only be included in capital under the transitional arrangements of CRD IV.

Tier 2 capital – An element of regulatory capital comprising the Group's collective impairment allowance and certain regulatory deductions made for the purposes of assessing capital adequacy.

Wholesale funding – The total of amounts owed to credit institutions, amounts owed to other customers and debt securities in issue.

Head Office: 2 Providence Place, West Bromwich B70 8AF.
www.westbrom.co.uk

Registered Number: 651B

Calls and electronic communications may be monitored and/or recorded for your security and may be used for training purposes. Your confidentiality will be maintained. The West Brom is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and Prudential Regulation Authority. Register No. 104877. 'the West Brom' is a trading name of West Bromwich Building Society.

the West Brom

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