

## LISTING PARTICULARS dated 10 April 2018

**THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION.** If you are in doubt as to the action you should take in connection with this document or the proposals contained in it, you are recommended to seek your own personal financial advice immediately from your stockbroker, bank manager, solicitor, accountant or other independent financial adviser authorised under the Financial Services and Markets Act 2000, if you are taking advice in the United Kingdom, or from another appropriately authorised independent financial adviser if you are taking advice in a jurisdiction outside the United Kingdom.

This document comprises listing particulars (the **Listing Particulars**) relating to West Bromwich Building Society (the **Society**) and to the Society and its consolidated subsidiaries (the **Group**) prepared in accordance with Part IV of the Luxembourg law on prospectuses for securities dated 10 July 2005, as amended, and may only be used for the purpose for which they are published.

Capitalised terms used in this Listing Particulars which are not otherwise defined have the meanings given to them in "Part XXIII: Definitions".



### WEST BROMWICH BUILDING SOCIETY

*(incorporated in England and Wales under the UK Building Societies Act 1986, as amended, and regulated by the Prudential Regulation Authority and the Financial Conduct Authority with FCA Mutuals Public Register Number 651B)*

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#### Issue of

**1,288,813 Core Capital Deferred Shares of £1 each  
at an Issue Price of £100 per Core Capital Deferred Share  
(the CCDS)**

and

**£22,498,600 11.00 per cent. Subordinated Tier 2 Notes due 2038  
at an issue price of 100 per cent. of their principal amount  
(the Tier 2 Notes and, together with the CCDS, the Securities)**

**and admission of the Securities to the Official List of the Luxembourg Stock Exchange and to trading on the  
Euro MTF Market (the Euro MTF) of the Luxembourg Stock Exchange**

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Application has been made to the Luxembourg Stock Exchange for all of the Securities to be issued to be listed on the Official List of the Luxembourg Stock Exchange and to be admitted to trading on the Euro MTF. The Euro MTF is not a regulated market within the meaning of Directive 2014/65/EU (as amended, **MiFID II**). It is expected that admission to listing on the Official List and to trading on the Euro MTF (**Admission**) will become effective and that dealings will commence on 12 April 2018.

**No application has been, or is currently intended to be, made for the Securities to be admitted to listing or trading on any other stock exchange.**

The Society accepts responsibility for the information contained in these Listing Particulars and declares that, to the best of the knowledge of the Society (which has taken all reasonable care to ensure that such is the case), the information contained in these Listing Particulars is in accordance with the facts and contains no omission likely to affect its import.

**MiFID II professionals/ECPs only / no PRIIPs KID / COBS 22.2: The Securities are not intended to be offered or sold or otherwise made available to retail investors.** See "Restrictions on Marketing and Sales to Retail Investors" below.

**Prospective investors should read these Listing Particulars in their entirety and in particular "Part I: Risk Factors" on pages 9 to 48 of these Listing Particulars for a discussion of certain risks and other factors that should be considered in connection with an investment in the Securities.**

**Prospective investors should be aware that an investment in the Securities involves significant risk and that, if one or more of the risks described in these Listing Particulars were to occur, investors may lose all or substantially all of their investment in the Securities. The CCDS and the Tier 2 Notes are financial instruments with complex features. As a provider of loss-absorbing capital to the Society, an investor in the Securities should be prepared to suffer losses on its investment if, in particular, the Society and/or the financial sector generally approaches or enters into a period of financial stress. In particular, investors should note that the Society has neither an obligation nor any right to redeem the CCDS and investors will not have any right to require the Society to redeem the CCDS or the Tier 2 Notes. The declaration of any interim and/or final Distribution on the CCDS by the Society in respect of any financial year is wholly discretionary.**

A transfer of CCDS will not be valid unless the number of CCDS transferred is a whole number that is equal to or greater than the minimum transfer amount prevailing at the time of transfer. The initial minimum transfer amount is fixed at 500 CCDS and will not be reduced except in agreement with the Relevant Regulators.

The Securities are being offered to professional investors holding existing capital instruments of the Society outside the United States in reliance on Regulation S under the Securities Act or another exemption from, or in a transaction not subject to, the registration requirements of the Securities Act. See paragraph 3 “*Selling Restrictions*” of “*Part VII: Distribution, Settlement and Transfers*”.

**The CCDS are deferred shares for the purposes of section 119 of the Building Societies Act 1986, as amended, and neither the CCDS nor the Tier 2 Notes are protected liabilities for the purpose of the Financial Services Compensation Scheme established under the FSMA.**

Recipients of these Listing Particulars are authorised solely to use it for the purpose of considering whether to subscribe for Securities pursuant to the Offers (as defined herein) and may not reproduce or distribute these Listing Particulars, in whole or in part, and may not disclose any of the contents of these Listing Particulars or use any information herein for any purpose other than considering an investment in the Securities pursuant to the Offers. Such recipients of these Listing Particulars agree to the foregoing by accepting delivery of these Listing Particulars.

**These Listing Particulars do not constitute or form part of any offer or invitation to sell or issue, or any solicitation of any offer to purchase or subscribe for, any securities other than the Securities to which they relate or any offer or invitation to sell or issue, or any solicitation of any offer to purchase or subscribe for, such Securities by any person in any circumstances in which such offer or solicitation is unlawful.**

No person has been authorised to give any information or make any representations other than those contained in these Listing Particulars and, if given or made, such information or representations must not be relied on as having been so authorised.

Neither the delivery of these Listing Particulars nor any subscription or sale made under them shall, under any circumstances, create any implication that there has been no change in the affairs of the Society or the Group since the date of these Listing Particulars or that the information in them is correct as of any subsequent time.

**IN MAKING AN INVESTMENT DECISION, EACH INVESTOR MUST RELY ON ITS OWN EXAMINATION, ANALYSIS AND ENQUIRY OF THE SOCIETY, THE TERMS OF THE OFFERS AND THE TERMS OF THE SECURITIES, INCLUDING THE MERITS AND RISKS INVOLVED.**

The Society is acting solely and exclusively in the capacity of issuer in respect of the Securities and is not acting for or on behalf of prospective investors or any other person, and will not regard any person (including any recipient or reader of these Listing Particulars or any actual or prospective investor in any of the Securities) as its “client” in relation to the offer or issue of the Securities or for any other purpose in connection therewith, and will not be responsible to any person for providing the sorts of protections afforded to persons who receive investment services or advice under the FSMA, MiFID II or any other regulatory regime in a capacity as a client.

Each investor, by its subscription of any Securities pursuant to the Offers, acknowledges that: (i) it has relied only on the information contained in these Listing Particulars; and (ii) no person has been authorised to give any information or to make any representation concerning the Society, the Group or the Securities (other than as contained in these Listing Particulars) and, if given or made, any such other information or representation should not be relied upon as having been authorised by the Society or any of its directors, officers, employees, agents or affiliates.

**The contents of these Listing Particulars should not be construed as legal, financial, accounting or tax advice. Each prospective investor should consult its own legal, financial, accounting or tax adviser for legal, financial, accounting or tax advice in relation to a purchase of Securities.**

#### **Notice to overseas investors**

The Securities have not been, nor will they be, registered under the United States Securities Act of 1933, as amended (the **Securities Act**) or under the applicable securities laws or the regulations of any state or other jurisdiction of the United States. The Securities are being offered and sold outside the United States in reliance on Regulation S under the Securities Act (**Regulation S**). Subject to certain exceptions, the Securities may not be offered or sold in the United States, Australia, South Africa, Japan, Hong Kong, Singapore, Italy, Switzerland or Canada. See paragraph 3 “*Selling Restrictions*” of “*Part VII: Distribution, Settlement and Transfers*”.

The Securities are subject to restrictions on resale and may not be transferred or resold except as permitted under applicable securities laws and regulations. Investors should be aware that they may be required to bear the financial risks of this investment for an extended or indefinite period of time.

**EACH PROSPECTIVE INVESTOR MUST BE OUTSIDE THE UNITED STATES AND MUST READ AND ENSURE THAT IT UNDERSTANDS THE MARKETING AND SALE RESTRICTIONS ON THE FOLLOWING TWO PAGES AND BE ABLE TO GIVE THE CONFIRMATION ON THE SECOND PAGE BEFORE REVIEWING THE REMAINDER OF THESE LISTING PARTICULARS OR MAKING ANY INVESTMENT DECISION IN RESPECT OF THE CCDS AND/OR THE TIER 2 NOTES.**

## RESTRICTIONS ON MARKETING AND SALES TO RETAIL INVESTORS

**MiFID II product governance / professional investors and ECPs only target market** – Solely for the purposes of the manufacturer's product approval process, the target market assessment in respect of the Securities has led to the conclusion that: (i) the target market of the Securities is 'eligible counterparties' and 'professional clients' only, each as defined in MiFID II; and (ii) all channels for the distribution of the Securities to eligible counterparties and professional clients are appropriate. Any person subsequently offering, selling or recommending the Securities (a **distributor**) should take into consideration the manufacturer's target market assessment; however, a distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Securities (by either adopting or refining the manufacturer's target market assessment) and determining appropriate distribution channels.

**PRIIPs Regulation / prohibition of sales to EEA retail investors** – The Securities are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area (**EEA**). For these purposes, a **retail investor** means a person who is one (or more) of: (i) a 'retail client' as defined in point (11) of MiFID II; or (ii) a customer within the meaning of Directive 2002/92/EC, where that customer would not qualify as a 'professional client' as defined in point (10) of Article 4(1) of MiFID II. No key information document required by Regulation (EU) No 1286/2014 (the **PRIIPs Regulation**) for offering or selling securities falling within scope of the PRIIPs Regulation or otherwise making them available to retail investors in the EEA has been prepared and therefore offering or selling the Securities or otherwise making them available to any retail investor in the EEA may, if the Securities were to be determined to fall within the scope of the PRIIPs Regulation, be unlawful under the PRIIPs Regulation.

**COBS 22.2 / restriction on marketing and sales to retail investors** - The Securities are financial instruments with complex features, and will not be a suitable or appropriate investment for all investors. The offer, sale or distribution of the Securities to certain investors, including retail investors, may be restricted or prohibited by law in certain jurisdictions. In particular, in June 2015, the UK Financial Conduct Authority (the **FCA**) published the Product Intervention (Contingent Convertible Instruments and Mutual Society Shares) Instrument 2015, which took effect from 1 October 2015 (the **Product Intervention Instrument**). Under the rules contained in the Product Intervention Instrument and Chapter 22.2 of the Conduct of Business Sourcebook (**COBS 22.2**) in the FCA's Handbook (as such rules may be amended or replaced from time to time, the **Product Intervention Rules**), there are restrictions on the sale of 'mutual society shares' (which would include the CCDS) to 'retail clients' in the EEA. For these purposes, a **retail client** is a person who is, or who if he were receiving services in the course of a firm carrying on a regulated activity would be, a client who is neither a 'professional client' nor an 'eligible counterparty' under MiFID II. Such restrictions may, absent an applicable exemption and depending on the nature of the relevant transaction with the retail client, require (amongst other things) the provision to the retail client of prescribed risk warnings, obtaining from the retail client certain confirmations and signed statements relating to the investment, limits on the amount of investments relative to a retail client's net assets and an assessment of whether the investment in the mutual society share is appropriate for the retail client.

The Society is required to comply with the Product Intervention Rules and COBS 22.2. Given the nature of the restrictions contained in the Product Intervention Instrument and COBS 22.2, the offer of CCDS described in these Listing Particulars is not made to retail clients (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2), and the Society will not offer or sell CCDS to retail clients, nor will the Society at any time take, or be required to take, any action which would facilitate an offer or sale of any CCDS to any retail client. By purchasing, or making or accepting an offer to purchase, any CCDS (or a beneficial interest therein) from the Society, each prospective investor represents, warrants, agrees with, and undertakes to, the Society that:

1. it is not a 'retail client' (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA;
2. whether or not it is subject to the Product Intervention Rules, it will not:
  - (A) sell or offer the CCDS (or any beneficial interest therein) to retail clients (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA; or
  - (B) communicate (including the distribution of these Listing Particulars) or approve an invitation or inducement to participate in, acquire or underwrite the CCDS (or any beneficial interests therein) where that invitation or inducement is addressed to or disseminated in such a way that it is likely to be received by a retail client (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA,

in any such case other than:

- (i) in relation to any sale or offer to sell CCDS (or any beneficial interest therein) to a retail client in or resident in the United Kingdom (the **UK**), in circumstances that do not and will not give rise to a contravention of the applicable Product Intervention Rules or COBS 22.2 by any person; and/or
- (ii) in relation to any sale or offer to sell CCDS (or any beneficial interest therein) to a retail client in any EEA member state other than the UK, where (a) it has conducted an assessment and concluded that (1) the relevant retail client understands the risks of an investment in the CCDS (or such beneficial interest therein), including if appropriate through the provision of appropriate risk warnings and the obtaining of all appropriate confirmations and statements from the retail client, and (2) the relevant retail client is able to bear the potential losses involved in an investment in the CCDS and (b) it has at all times acted in relation to such sale or offer in compliance with MiFID II to the extent it applies to it or, to the extent

MiFID II does not apply to it, in a manner which would be in compliance with MiFID II if it were to apply to it; and

3. it will at all times comply with all applicable laws, regulations and regulatory guidance (whether inside or outside the EEA) relating to the promotion, offering, distribution and/or sale of the CCDS (and any beneficial interest therein), including (without limitation) any such laws, regulations and regulatory guidance relating to determining the appropriateness and/or suitability of an investment in the CCDS (or any beneficial interest therein) by investors in any relevant jurisdiction.

Where acting as agent on behalf of a disclosed or undisclosed client when purchasing, or making or accepting an offer to purchase, any CCDS (or any beneficial interest therein) from the Society, the foregoing representations, warranties, agreements and undertakings will be given by and be binding upon both the agent and its underlying client.

**Confirmation of your representation:** In order to be eligible to view the remainder of these Listing Particulars or make an investment decision with respect to the Securities described herein, you must be an Eligible Person (as defined below) and must not be in the United States. By continuing to read these Listing Particulars, you represent and warrant to the Society that:

- (i) you are, and (if you are acting as an intermediary) each person for whom you are acting as intermediary and who is making an investment decision in respect of the Securities is, an Eligible Person;
- (ii) you are, and each person on whose behalf you are acting in connection with the Securities is, outside the United States and, to the extent you purchase any Securities, you will be purchasing Securities pursuant to Regulation S under the Securities Act;
- (iii) the electronic mail address to which the Listing Particulars have been delivered is not located in the United States, its territories and its possessions; and
- (iv) you consent to delivery of the Listing Particulars and any amendments or supplements thereto by electronic transmission.

An **Eligible Person** is a person satisfying all of the following criteria:

- (1) a person that, if such person were receiving services in the course of a firm carrying on a regulated activity, would be a client who is either a 'professional client' or an 'eligible counterparty' under MiFID II;
- (2) a 'qualified investor' within the meaning of Article 2(1)(e) of Directive 2003/71/EC, as amended; and
- (3) if it is in the United Kingdom, it is an 'investment professional' for the purposes of Article 19 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005.

#### **Additional Offer Restrictions**

In addition to the foregoing, the distribution of these Listing Particulars and the offer and sale of the Securities in certain jurisdictions may be restricted by law. These Listing Particulars must not be distributed, and no offer and sale of the Securities will be made, in the United States, Australia, South Africa, Japan, Hong Kong, Singapore, Italy, Switzerland or Canada. No action has been or will be taken by the Society to permit a public offering of the Securities, or possession or distribution of these Listing Particulars or any other offering or publicity material relating to the Securities, in any country or jurisdiction where action for that purpose is required. Accordingly, neither these Listing Particulars, any advertisement, nor any other offering material may be distributed or published in any jurisdiction except under circumstances that will result in compliance with any applicable laws and regulations. Persons into whose possession these Listing Particulars comes should inform themselves about and observe any such restrictions. Any failure to comply with applicable restrictions may constitute a violation of the securities laws of the relevant jurisdiction. Further information with regard to the restrictions on the distribution of these Listing Particulars and the offering and sale of the Securities is set out at paragraph 3 "*Selling Restrictions*" of "*Part VII – Distribution, Settlement and Transfers*".

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## IMPORTANT INFORMATION

**The Securities are financial instruments with complex features. As a provider of regulatory capital to the Society, an investor in CCDS and/or Tier 2 Notes should be prepared to suffer losses on its investment – which may mean losing all or substantially all of its investment - if, in particular, the Society and/or the financial sector generally approaches or enters into a period of financial stress.**

**Accordingly, the Securities are not intended to be offered or sold or otherwise made available to retail investors. See “*Restrictions on Marketing and Sales to Retail Investors*” above.**

Investors in CCDS should note that holders of CCDS have:

- no right to have their CCDS redeemed;
- no right to Distributions on the CCDS, the declaration of which by the Board is wholly discretionary, and Distributions are in any event subject to a cap and other restrictions;
- only limited, capped rights to a return on the winding-up of the Society, and in the event of an insolvent winding-up of the Society, no right to receive any return;
- no statutory, contractual or any other pre-emption rights; and
- no member voting rights in respect of their CCDS for so long as they are held through the Clearing Systems, as discussed below. For more information in relation to member voting rights, see paragraph 4 “*Meetings of the Members of the Society*” of “*Part VIII: Overview of Certain Provisions of the Rules of the Society and the Act relating to the Core Capital Deferred Shares*”.

CCDS are deferred shares for the purposes of section 119 of the Building Societies Act 1986, as amended (the **Act**), and are not protected liabilities of the Society for the purposes of (and holders of the CCDS will not therefore benefit from) the Government Financial Services Compensation Scheme.

Investors in Tier 2 Notes should note that holders of Tier 2 Notes will have:

- no right to have their Tier 2 Notes redeemed until 12 April 2038 (being the maturity date for the Tier 2 Notes);
- only limited enforcement rights, and a claim in the winding-up of the Society that is subordinated to most of the Society’s other liabilities; and
- no member voting rights.

As a provider of regulatory capital to the Society, an investor in the Securities should be prepared to suffer losses on its investment - which may mean losing all or substantially all of its investment - if, in particular, the Society and/or the financial sector generally approaches or enters into a period of financial stress. Such losses could be manifested in a number of ways, including (without limitation) that:

- the Society may elect or may be required by law or by the PRA (or any successor or other authority having primary supervisory authority with respect to prudential matters in relation to the Society) to cease declaring Distributions (or reduce the amount declared) on CCDS either on a temporary or a permanent basis and at any time or whilst any specified circumstances (as referred to below) subsist or during a specified period;
- the market price of the CCDS and the Tier 2 Notes may fall significantly;

- further CCDS or other instruments may be issued which dilute (either initially or upon conversion into CCDS) the holdings of CCDS investors, and there is no limit on the amount of liabilities which the Society may incur ranking senior to the CCDS and the Tier 2 Notes; and
- in a worst-case scenario, the UK authorities could take action under the Banking Act 2009 (or similar future legislation) or the Society could enter into an insolvent winding-up,

with the result that investors in the CCDS and the Tier 2 Notes could lose all or substantially all of their investment in the Securities.

**The Society does not currently anticipate paying any Distributions in respect of the CCDS in respect of the financial years ended 31 March 2018 and 31 March 2019, and any Distributions thereafter will be subject to, amongst other things, the Society’s financial performance and the discretion of the Board.** See “Part V – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy – 3. Distribution Policy in respect of the CCDS” below. There are also a number of circumstances in which the Society may be prevented from paying or be required to cease paying Distributions. These circumstances include the fact that:

- the Society is not permitted to, and will not, declare a Distribution that is greater than the amount of profits and reserves (if any) of the Society which are available, in accordance with applicable law and regulation then prevailing, for the payment of such Distribution;
- under Article 141 of CRD IV, the Society will not be permitted to declare Distributions to an extent which would decrease its Common Equity Tier 1 capital to a level where the combined buffer requirement (the total Common Equity Tier 1 capital to meet the capital conservation buffer and countercyclical buffer requirements) is not met and, if at any point the Society fails to maintain sufficient Common Equity Tier 1 capital to meet the combined buffer requirement, it will not be permitted to pay any Distributions in excess of a ‘maximum distributable amount’ calculated in accordance with Article 141; and
- the total Distribution declared on each CCDS in respect of any given financial year of the Society is subject to a cap.

Further, there can be no assurance that a secondary market in the Securities will be established. Even if a secondary market does operate, it may be illiquid, the market price of the Securities may be volatile, and prices may go down as well as up. Given the uncertainty as to the secondary trading market, that the CCDS are perpetual instruments and the Society has no obligation to redeem or repurchase them, and the Tier 2 Notes do not mature until 2038 and the Society has no obligation to redeem or repurchase them before that time, an investor should be prepared to hold any Tier 2 Notes for an extended duration and any CCDS for an indefinite period of time.

The CCDS are also subject to a minimum transfer amount of 500 CCDS which is fixed and will not be reduced except in agreement with the Relevant Regulators. The Society has no current intention to seek the request of the Relevant Regulators to reduce the minimum transfer amount.

Each investor in the Securities should determine the suitability of such investment in light of its own circumstances, either on its own or with the help of its financial and other professional advisers. In particular, each potential investor should:

- have sufficient knowledge and experience to make a meaningful evaluation of the Securities, the merits and risks of investing in the Securities and the information contained or incorporated by reference in these Listing Particulars;
- have access to, and knowledge of, appropriate analytical tools to evaluate, in the context of its particular financial situation, an investment in the Securities and the impact the Securities will have on its overall investment portfolio;

- have sufficient financial resources and liquidity to bear all of the risks of an investment in the Securities, including where such potential investor's financial activities are principally denominated in a currency other than pounds sterling, and the possibility that the entire investment in the Securities could be lost, including following the exercise of any bail-in power by the resolution authorities under the Banking Act 2009; and
- be able to evaluate (either alone or with the help of a financial adviser) possible scenarios for economic, interest rate and other factors that may affect its investment and its ability to bear the applicable risks.

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent: (i) the Securities are legal investments for it; (ii) the Securities can be used as collateral for various types of borrowing; and (iii) other restrictions apply to its purchase or pledge of any Securities. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of the Securities under any applicable risk-based capital or similar rules.

Securities must be held through an account (or through an institution which has an account) with Euroclear and/or Clearstream, Luxembourg or any replacement or successor clearing system (together, the **Clearing Systems**). This requirement applies for so long as Euroclear or Clearstream, Luxembourg remain in business and even if Euroclear and Clearstream, Luxembourg both cease to carry on business, will apply so long as there is a successor or alternative clearing system available. There are certain consequences for holders of this requirement which are discussed in "*Part I: Risk Factors*".

The Society considers that it is unlikely that there will not be a Clearing System through which the Securities can be held. However, should this be the case, each investor would at the appropriate time receive a Securities certificate registered in its name.

Any investor who is in any doubt as to the suitability of the Securities as an investment should take professional advice.



## PART I – RISK FACTORS

*Any investment in the Securities is subject to a number of risks, most of which are contingencies which may or may not occur, and the Society is not in a position to express a view on the likelihood of any such contingency occurring or the extent of the likely impact.*

*Prior to investing in the Securities, prospective investors should carefully consider the risk factors associated with any investment in the Securities, the Society and the financial services industry in the UK in general, together with all the other information contained in this document. This section describes the risk factors which are considered by the Society to be material to it and an investment in the Securities. However, these should not be regarded as a complete and comprehensive statement of all potential risks and uncertainties. There may be other risks and uncertainties which are currently not known to the Society or which the Society currently does not consider to be material. Should any of the risks described below, or any other risks or uncertainties, occur this could have a material adverse effect on the Society's business, results of operation, financial condition or prospects which in turn would be likely to affect the Society's ability to make Distributions in respect of the CCDS and/or satisfy its obligations under the Tier 2 Notes and/or cause the price of the Securities to decline and, as a result, an investor in the Securities could lose some or all of its investment.*

*This section of the Listing Particulars is divided into five sections – “Risks related to the Society's business”, “Regulatory Risks”, “Risks Related to the CCDS”, “Risks Related to the Tier 2 Notes” and “Risks Related to all Securities”.*

### 1. RISKS RELATED TO THE SOCIETY'S BUSINESS

#### UK macro-economic environment and outlook

The Society is exclusively focused in the UK and, therefore, the general UK macro-economic environment is key to its success. As a consequence, the Society's operating results, financial condition and prospects are significantly affected by the general economic conditions in the UK economy and the economic confidence of consumers and businesses.

The outlook for the UK economy is uncertain, particularly in light of the UK's decision to leave the European Union. Adverse changes to the operating environment arising from the general uncertainty in the UK economy could lead 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;
- a fall in consumer confidence impacting adversely consumer spending and weakening the strength of UK retailers;
- increased competition for and cost of retail funding; and
- low or flat economic growth.

The Society's 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.

Adverse changes and uncertainty in UK economic conditions could lead to a decline in the credit quality of the Society's borrowers and counterparties and have an adverse effect on the quality of the Society's loan portfolio, which could result in a rise in delinquency and default rates, reduce the recoverability and value of the Society's assets and require an increase in its level of provisions for bad

and doubtful debts. Likewise, a significant reduction in the demand for the Society's products and services could negatively impact its business and financial condition.

There remains a risk that if low inflation or deflation becomes entrenched in the UK, consumer spending and wage growth will be dampened. These pressures on households may lead to an increase in arrears in the Society's residential mortgage lending portfolio, and an associated increase in impairment. There can be no assurance that the Society will not have to increase its provisions for loan losses in the future as a result of increases in non-performing loans and/or for other reasons beyond its control. Material increases in the Society's provisions for loan losses and write-offs/charge-offs could have an adverse effect on its operating results, financial condition and prospects.

Government policies and the Bank of England (the **BoE**) action of cutting interest rates and increasing quantitative easing provisions, as well as measures such as the Funding for Lending Scheme (**FLS**) and Term Funding Scheme (**TFS**), have ensured that the low interest rate environment has continued to stimulate the housing market, although this has contributed to highly competitive mortgage pricing. The stimulus provided by the TFS scheme, providing low cost four year funding, would appear to have had a marked impact on mortgage and saving markets in 2017 with this expected to continue in 2018. As at 28 February 2018, when the TFS closed, approximately £127 billion had been drawn under the scheme. These very large volumes of low cost funding would appear to have resulted in some distortion in normal market pricing. Although the BoE Bank Rate increased in November 2017, the mortgage rates offered by many lenders have actually reduced since November. It may take a number of months for the low cost funding provided by TFS to work its way through the financial system. During this period mortgage pricing may remain particularly competitive, with an adverse impact on the profitability of new lending that is not utilising the low cost TFS funding.

Later in 2018, once TFS funding has been utilised, mortgage rates may increase, particularly if the lower value of sterling prompts a series of increases in interest rates from the BoE to counter inflation. In such a scenario, other market participants might offer more competitive product pricing resulting in increased customer attrition for the Society. A further risk from sterling currency devaluation is likely to be an increase in the cost of imported goods and services, which could affect customers' ability to make mortgage payments if wage inflation does not keep track with the Consumer Price Index (**CPI**).

A rise in mortgage rates could result in a slowdown in the housing market. This could produce a further squeeze of mortgage margins, with lenders seeking to maintain volumes in a shrinking market which could result in increased customer attrition for the Society.

Additionally, house price growth has been accelerating faster than earnings, with housing affordability becoming more stretched. There is a risk that house price growth could outstrip earnings and reduce demand for new mortgages in the future. In addition, any increase in interest rates will increase mortgage payments, which could lead to higher residential loan losses.

A weakening of the UK economy could result in higher unemployment and a consequent loss of public confidence in the UK economy. This could have the effect of reducing consumer demand for new mortgage lending, resulting in the Society's lending targets becoming unachievable, as well as increasing potential credit losses in the Society's mortgage portfolios.

Worsening economic conditions in the UK could result in a weakening tenant performance and create uncertainty in relation to the cash flows of the Society's borrowers in the commercial real estate market and in relation to the value of their collateral. The Society's non-core commercial loan book has historically proven sensitive to a downturn in the economic environment. While the Group's exposure to this sector is steadily reducing, there remains the risk of further commercial impairment provision being required which would impact adversely the Society's financial and operational performance.

Downward pressure on profitability and growth could occur as a result of a number of external influences, such as the consequences of a more austere economic environment and the impact of global

economic forces on the UK economy. Adverse changes in global growth may pose the risk of a further slowdown in the UK's principal export markets, which would have an adverse effect on the broader UK economy.

#### **Global financial markets and general economic conditions in the Eurozone and internationally**

The Society is directly and indirectly subject to inherent risks arising from general economic conditions in the UK and other economies, particularly the Eurozone. The dislocations in financial markets that have occurred since the global financial crisis of 2007-2008 were accompanied by recessionary conditions and trends in the UK and a period of significant turbulence and uncertainty for many financial institutions in the UK and around the world, including the Society and many of its counterparties. Any future disruptions could again pose systemic risks that negatively affect, among other things:

- consumer confidence;
- levels of unemployment;
- the state of the UK housing market and the commercial real estate sector;
- bond and equity markets;
- counterparty risk;
- the availability and cost of credit;
- transaction volumes in wholesale and retail markets including the availability and duration of funding in wholesale markets;
- the liquidity of the global financial markets; and
- market interest rates, including interest rate rises and the associated impact on affordability,

which in turn could have a material adverse effect on the Society's business, operating results, financial conditions and prospects.

In the Eurozone, high levels of private and public debt, outstanding weaknesses in the financial sector and reform fatigue, are a concern. The possibility of prolonged low growth in the Eurozone could inhibit the UK's own economic recovery, given the extensive economic and financial linkages between the UK and the Eurozone. The UK's trade and current account balances with the Eurozone would be likely to deteriorate further, negatively affecting UK growth. The possibility of a sovereign default and the managed or unanticipated exit of one or more member states from the European Monetary Union could also pose a threat to the stability of financial markets and could cause other risks.

Global stresses, both economic and political, in particular in the Eurozone, may have a detrimental effect on the UK economy and could adversely affect the Society's business by reducing the level of demand for, and supply of, the Society's products and services. This could expose the Society to lower asset and other realisations, and increased negative fair value adjustments and impairments of investments and other assets and may materially and adversely impact the Society's operating results, financial condition and prospects.

Although, globally and in the UK, economic and financial market conditions have generally stabilised in recent years, there have been periods of significant volatility in financial markets around the world. This generally has led to more difficult business conditions for the financial sector. Continued or worsening disruption and volatility in the global financial markets could have a material adverse effect

on the Society, including on its ability to access liquidity on financial terms acceptable to it, if at all. Any such reduction in availability of funding or increase in deposit rates could have a material adverse effect on the Society's interest margins, liquidity and profitability.

### **Risks in relation to the United Kingdom's vote to leave the European Union**

On 23 June 2016 the UK voted to leave the European Union in a referendum (the **Brexit Vote**) and on 29 March 2017 the UK gave formal notice (the **Article 50 Notice**) under Article 50 of the Treaty on European Union (**Article 50**) of its intention to leave the European Union. The timing of the UK's exit from the EU remains subject to some uncertainty, but it is unlikely to be before the end of March of 2019. Article 50 provides, subject to certain circumstances, that the EU treaties will cease to apply to the UK two years after the Article 50 Notice. The terms of the UK's exit from the EU are also unclear and will be determined by the negotiations taking place following the Article 50 Notice. It is possible that the UK will leave the EU with no withdrawal agreement if no agreement can be finalised before 29 March 2019. In such circumstances, it is likely that a high degree of political, legal, economic and other uncertainty will result. The Brexit Vote and delivery of the Article 50 Notice have resulted in political (including UK constitutional), legal, regulatory, economic and market uncertainty – the effects of each of which could adversely affect the Society. Such uncertainty and consequential market disruption may also cause investment decisions to be delayed, reduce job security and damage consumer confidence. The resulting adverse economic conditions could affect obligors' willingness or ability to meet their obligations, resulting in increased defaults in the mortgage portfolio and ultimately the profitability and prospects of the Society.

Furthermore, the Brexit Vote has resulted in downgrades of the UK sovereign and the BoE by S&P, Moody's and Fitch. S&P, Fitch and Moody's have all placed a negative outlook on the UK sovereign rating and that of the BoE, suggesting a strong possibility of further negative rating action. The rating of the sovereign affects the ratings of entities operating in its territory, and in particular the ratings of financial institutions. Further downgrades of the UK sovereign and the BoE may cause downgrades to key banking counterparties for the Society. If rating action is widespread, it may become difficult or impossible to replace counterparties with others who have suitable ratings. Moreover, a more pessimistic economic outlook for the UK in general could lead to increased concerns around the future performance of the Society's residential mortgage and commercial loan portfolios.

### **Political Risks within the Eurozone**

The exit of a member state from the European Union and/or European Monetary Union or significant failures or stress in the financial system in any member state could result in deterioration in the economic and financial environment in the UK and Eurozone that would materially affect the capital and the funding position of participants in the banking industry, including the Society. This could also give rise to operational disruptions to the Society's business. The effects on the European and global economy of the exit of one or more Eurozone member states or the redenomination of financial instruments from euro to a different currency, are impossible to predict and protect fully against in view of (i) economic and financial instability in the Eurozone, (ii) difficulties in predicting whether the current signs of recovery will be sustained and at what rate, (iii) the uncertain legal position and (iv) the fact that many of the risks related to the business are totally, or in part, outside the Society's control.

### **Risks from changes to monetary policy or interest rates, in the UK and abroad**

The prevailing level of interest rates and the provision or withdrawal of other accommodative monetary and fiscal policies, which are impacted by factors outside the Society's control, including the fiscal and monetary policies of governments and central banks, as well as UK and international political and economic conditions, affect the Society's results of operations, financial condition and return on capital.

Stimulus measures in the UK and elsewhere have been highly accommodative in recent years, including FLS, TFS and the Help to Buy scheme (**Help to Buy**), a Government scheme introduced in 2013 designed to enable buyers to put down a 5 per cent. deposit on a home with the Government guaranteeing up to 20 per cent. of the mortgage (40 per cent. in London) funded by a commercial lender. Such measures have helped to support demand at a time of fiscal tightening and balance sheet repair. The relatively long period of stimulus in the UK and elsewhere has increased uncertainty over the impact of its reduction, which could lead to generally weaker than expected growth, or even contracting GDP, reduced business confidence, higher levels of unemployment or underemployment, adverse changes to levels of inflation, potentially higher interest rates and falling property prices in the markets in which the Society operates, and consequently to an increase in delinquency rates and default rates among the Society's customers. Moreover, higher prevailing interest rates would affect the Society's cost of funding from depositors and creditors, which could adversely affect its profitability, to the extent its margins decline.

The personal sector in the UK remains heavily indebted and vulnerable to increases in unemployment, rising interest rates and/or falling house prices. As a result of, among other factors, increases and decreases in the BoE Bank Rate, interest rates payable on a significant portion of the Society's outstanding mortgage loan products, particularly the Society's Buy-to-Let portfolio, fluctuate over time. Rising interest rates would put pressure on borrowers whose loans are linked to the BoE Bank Rate because such borrowers may experience financial stress in repaying at increased rates in the future. A significant portion of the Society's outstanding mortgage loan products are potentially subject to changes in interest rates, resulting in borrowers with a mortgage loan subject to a variable rate of interest or with a mortgage loan for which the related interest rate adjusts following an initial fixed rate or low introductory rate, as applicable, being exposed to increased monthly payments as and when the related mortgage interest rate adjusts upward (or, in the case of a mortgage loan with an initial fixed rate or low introductory rate, at the end of the relevant fixed or introductory period). Since 2009, both variable and fixed interest rates have been at relatively low levels, which have benefited borrowers taking out new loans and those repaying existing variable rate loans, regardless of special or introductory rates, and these rates are expected to increase as and when general interest rates return to historically more normal levels. Future increases in borrowers' required monthly payments, which (in the case of a mortgage loan with an initial fixed rate or low introductory rate) may be compounded by any further increase in the related mortgage interest rate during the relevant fixed or introductory period, ultimately may result in higher delinquency rates and losses in the future.

In an increasing interest rate environment, borrowers seeking to avoid these increased monthly payments by refinancing their mortgage loans may no longer be able to find available replacement loans at comparably low interest rates. Increased unemployment could lead to borrowers who are made redundant being unable to service the loan payments in a timely fashion which would result in higher levels of arrears in the Society's residential mortgage loan portfolio which, in turn, would lead to an increase in its impairment charges in respect of this portfolio. Declines in housing prices may also leave borrowers with insufficient equity in their homes to permit them to refinance. These events, alone or in combination, may contribute to higher delinquency rates and losses.

Conversely, there are risks associated with a continuation of the sustained low interest rate environment or further reductions in interest rates in the UK or other major developed economies, including if the BoE were to lower its target rate to a negative rate (as other major central banks, including the European Central Bank and the Bank of Japan, have done). A prolonged period of low interest rates could further reduce incentives for the Society's customers to save, reducing Society's funding from deposits. Additionally, the low interest rate environment has and may continue to put pressure on net interest income and margins throughout the UK financial industry. The Society's business, financial performance, net interest income and margin may continue to be adversely affected by the low interest rate environment.

## **United Kingdom Property Market**

One of the Society's primary activities is mortgage lending in the UK with loans secured against residential and commercial property. A downturn in the UK economy could have a negative effect on the housing market which, combined with an increased level of unemployment and arrears rates, could give rise to higher provisions for credit losses being incurred by the Society.

Property prices may fall and could result in losses being incurred by lenders on loans that have defaulted. Any significant fall in the UK residential property prices could have consequences for the Society's funding costs if there were deemed to be a material deterioration in the quality of its mortgage portfolios.

The Society, via a subsidiary business (West Bromwich Homes Limited), invests in residential property creating a further exposure to the UK housing market, where there is a 38% concentration of properties in Wales. Falling house price measures (such as the House Price Index (**HPI**)) could lead to a reduction in the book value of West Bromwich Homes Limited properties. Revaluation gains of £5.4 million were reported for the West Bromwich Homes Limited residential property portfolio in FY 2017 (£5.5 million FY 2016) as a result of positive house price inflation, and revaluation losses could be reported should HPI turn negative.

The residential mortgage lending market in the UK is competitive, and developments in this market, and increased competition, could have an adverse effect on the Society's position in the market, and therefore on the Society's financial position.

The commercial property book is highly sensitive to any worsening in the economic climate and a fall in commercial property prices could lead to increased provisions for credit losses. Low or flat economic growth could lead to further tenant failures in the Group's commercial loan portfolio. The Society has pursued a strategy of managing down exposure to commercial real estate, although a full exit is still expected to be more than 10 years away. The remaining exposure has a concentration in the retail sector which is particularly susceptible to changes in rental levels achievable. Should rental levels fall there would be a material impact on the impairment provisions required.

### ***The Society's Mortgage Portfolios***

#### *Default by borrowers in paying amounts due on their mortgage loans*

Borrowers may default on their obligations under their mortgage loans. Defaults may occur for a variety of reasons. The mortgage loans are affected by credit, liquidity and interest rate risks. Various factors influence mortgage delinquency rates, prepayment rates, repossession frequency and the ultimate payment of interest and principal, such as changes in the national or international economic climate, regional economic or housing conditions, changes in tax laws, interest rates, inflation, the availability of financing, yields on alternative investments, political developments and government policies.

Other factors in borrowers' personal or financial circumstances may affect the ability of borrowers to repay the mortgage loans. Unemployment, loss of earnings, illness, divorce and other similar factors may lead to an increase in delinquencies by and bankruptcies of borrowers, and could ultimately have an adverse impact on the ability of borrowers to repay the mortgage loans. In addition, the ability of a borrower to sell a property given as security for a mortgage loan at a price sufficient to repay the amounts outstanding under that mortgage loan will depend upon a number of factors, including the availability of buyers for that property, the value of that property and property values in general at the time.

If a borrower fails to repay its mortgage loan and the related property is repossessed, the likelihood of there being a net loss on disposal of the property is increased.

In order to enforce a power of sale in respect of a property, the relevant mortgagee must first obtain possession of the relevant property. Possession is usually obtained by way of a court order or decree. This can be a lengthy and costly process and will involve the mortgagee assuming certain risks. In addition, once possession has been obtained, a reasonable period must be allowed for marketing the property, to discharge obligations to take reasonable care to obtain the best price.

#### *Declining property values*

The value of the mortgaged properties may be affected by, among other things, a decline in the residential or commercial property values in the UK. If the residential or commercial property market in the UK should experience an overall decline in property values, such a decline could in certain circumstances result in the value of the mortgaged properties being significantly reduced and may result in losses.

The Society cannot guarantee that the value of a property will remain at the same level as on the date of origination of the related mortgage loan. Any downturn in the UK economy may have a negative effect on the housing market. Any fall in property prices resulting from deterioration in the housing market could result in losses being incurred by lenders where the net recovery proceeds of a sale are insufficient to redeem the outstanding loan.

Should residential property values decline further, borrowers may have insufficient resources to refinance their mortgage loans with lenders other than the originator and may have insufficient resources to pay amounts in respect of their mortgage loans as and when they fall due. This could lead to higher delinquency rates and losses which in turn may adversely affect the Society.

#### *Increases in prevailing market interest rates may adversely affect the performance of the loan portfolio*

Although interest rates are currently at a low level relative to that observed historically, this may change in the future and an increase in interest rates may adversely affect borrowers' ability to pay interest or repay principal on their mortgage loans. Borrowers with a mortgage loan subject to a variable rate of interest will be exposed to increased monthly payments if the related mortgage interest rate adjusts upward. Borrowers of a mortgage loan with an initial fixed rate or low introductory variable rate will be exposed to increased monthly payments at the end of the relevant fixed or introductory period. This increase in borrowers' monthly payments at the end of an initial fixed or low introductory period may be compounded by any further increase in the related mortgage interest rate during the relevant fixed or introductory period. Whilst the Society seeks to mitigate this risk by stressing the impact of higher interest rates when assessing the borrower's affordability by assuming that the interest rate to which the borrower reverts after their initial fixed or discounted period, normally the Society's Standard Variable Rate (SVR), could rise by 3%, there can be no assurance that this will mitigate default levels. Further, should interest rates increase beyond this stressed level, default levels would be likely to increase significantly.

Borrowers seeking to avoid increased monthly payments (caused by, for example, the expiry of an initial fixed rate or low introductory rate, or a rise in the related mortgage interest rates) by refinancing their mortgage loans may no longer be able to find available replacement loans at comparably low interest rates. Any decline in housing prices may also leave borrowers with insufficient equity in their homes to permit them to refinance.

These events, alone or in combination, may contribute to higher delinquency rates and losses on the Society's mortgage portfolios.

#### *Geographic Concentration Risks*

Mortgage loans in the Society's mortgage portfolios may be subject to geographic concentration risks. To the extent that specific geographic regions within the UK have experienced or may experience in

the future weaker regional economic conditions and housing markets than other regions in the UK or a particular region experiences a natural disaster, a concentration of the mortgage loans in such a region may be expected to exacerbate certain of the risks relating to the mortgage loans described in this section.

#### *Use of intermediaries for re-mortgaging*

It is now common practice for mortgage intermediaries to play an active role in re-mortgaging as mortgage products come to the end of their incentive periods. A consequence of this could be reduced retention and lower reversion rates. The shorter average life of the mortgages could have an adverse impact on profitability.

#### **Retail funding and competition risks**

The Society is primarily funded by retail deposits, with residential mortgage assets at 31 March 2017 covered 1.04 times by retail savings balances.

The maintenance and growth of the Society's lending activities depends in large part on the availability of retail deposit funding on appropriate terms. Increases in the cost of such funding in the wake of the financial crisis together with the low BoE Bank Rate environment have had a negative impact on the Society's margins and profit. Such pressures could sustain for an extended period or re-emerge and, in extreme circumstances, a loss of consumer confidence could result in high levels of withdrawals from the Society's retail deposit base, upon which it relies for lending and which could have a material adverse effect on the Society's business, financial position and results of operations.

In an extreme scenario the Society may not be in a position to continue to operate without additional funding support. Inability to access such support could have a material impact on the Society's solvency. These risks can be exacerbated by many factors, including an over-reliance on a particular source of funding or market-wide phenomena such as market dislocation and major disasters. There is also a risk that the funding structure employed by the Society may prove to be inefficient, giving rise to a level of funding cost that is not sustainable in the long term for the Society to grow its business or even maintain it at current levels. The Society's ability to access retail and wholesale funding sources on satisfactory economic terms is subject to a variety of factors, including a number of factors outside its control, such as liquidity constraints, general market conditions, regulatory requirements and loss of confidence in the UK banking system.

Increasing competition in the personal financial services market may adversely affect the Society's income and business. Historically, increased competition has resulted in downward pressure on the industry's spread between deposit and loan rates. Further increases in competition, including by the new 'challenger' banks that are offering competitive rates and are able to operate from a lower operating cost base under their business models, may negatively affect the Society's financial position and the benefit it is able to return to its members. In addition, recent technological advances have allowed new competitors to emerge both from within the traditional financial services arena and from outside it, and continued advances in technology may lead to further new entrants.

On 9 August 2016, the Competition and Markets Authority (the **CMA**) published a final report following its market investigation into competition in the personal current accounts and the small and medium-sized enterprises retail banking markets in the United Kingdom. The report identified features of the markets for the supply of personal current accounts, business current accounts and SME lending that are having an adverse effect on competition. The CMA decided on a comprehensive package of remedial measures, which were introduced in the Retail Banking Market Investigation Order 2017. These measures, together with changes to the payment services directive (**PSD2**) are commonly referred to as Open Banking. There are risks and uncertainties from regulatory changes such as Open Banking and ring fencing of the major UK banks, particularly the resulting impact on the competitive environment. Open Banking has the potential to disrupt significantly traditional personal financial



services models and provides challenges for long-established banks by increasing competition and requiring that these banks invest in new technology. Whilst the Society does not operate current accounts and is not directly impacted by PSD2, Open Banking could result in the emergence of new competitors, potentially with substantially different business models that materially alter the competitive environment and this could affect the Society's ability to attract and retain customers, adversely affecting liquidity and increasing its funding costs over time.

Implementation of ring fencing is expected to result in increased activity from the larger banks on the UK domestic market. Their activity may result in pressure on margins in the markets in which the Society operates.

The rise of digital banking is changing customer expectations of the availability of banking services. As digital changes make transactions easier and more convenient, the Society expects customers to transact more, and in many different ways. The Society may not be able to manage service provision ahead of rising customer expectations or may have competitors who are more successful in meeting demand for digital banking services.

In addition, if the Society's customer service levels are perceived by the market to be materially below those of competitor UK financial institutions, it could lose existing and potential new business. If the Society is not successful in retaining and strengthening customer relationships, it may lose market share, incur losses on some or all of its activities or fail to attract new deposits or retain existing deposits, which could have a material adverse effect on its business, financial condition and results of operations.

The Society holds buffer eligible liquidity over and above the requirements laid down by the BoE acting as Prudential Regulation Authority through its Prudential Regulation Committee (the **PRA**) and these are under continuous review. The Society maintains liquid assets of a suitable quality known as High Quality Liquid Assets, in order to ensure all its liquidity indicators are well above the required regulatory limits. These include the Liquidity Coverage Ratio (**LCR**) and Net Stable Funding Ratio (**NSFR**). The Society has duration limits in place to reflect the requirements of the latest update to the PRA Supervisory Statement 20/15 which came into force in January 2017.

### **Wholesale funding market risks**

Although the Society will remain predominantly funded by retail savings balances (and is required to do so under the Act), 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. Throughout 2016/17 there was a consolidation in the short-term unsecured money market, resulting in a reduced 'core' pool of counterparties continuing to provide liquidity. There has been a noticeable slowdown in the number of potential new funding providers entering this market. This has been attributed to various reasons, from a lack of available funds, increased credit requirements and a gradual move to managed money market funds and repurchase agreements. The long-term secured and unsecured wholesale funding markets have been subject to prolonged periods of volatility, particularly following the Brexit Vote and the resultant market uncertainty. The market has experienced periods of virtual closure in the past as well as prohibitive pricing which has factored in the perceived additional risks to potential investors for new external issuances of securities.

In 2018, there is an ongoing risk that volatility in wholesale markets could increase. This could result in potential issuances in these markets being uncertain both in volume and price. The Society will continue to manage its funding requirements through a combination of retail, wholesale and long-term capital market issuances. These are supplemented by participation in central bank support facilities, in particular the BoE Indexed Long Term Repo Facility and the TFS announced in 2016. The Society, along with other financial institutions, has taken advantage of this opportunity to obtain low cost term funding.

These BoE facilities have added substantial additional liquidity to the markets, resulting in greatly improved levels of liquidity for major UK banks and building societies. However, the Society does not have influence over the policy making behind such measures. Further, there can be no assurance that these conditions will not lead to an increase in the overall concentration risk and cost of funding of the Society or otherwise adversely affect the Society.

A number of other UK banks and building societies have availed themselves of the same measures as the Society and will be seeking to refinance their obligations as the various schemes mature. When such refinancing occurs, this may affect the Society's ability to access wholesale funding arrangements on satisfactory market terms in order to meet its continuing funding requirements and could have a material impact on the Society's liquidity. Whilst the Society has sought to mitigate the impact of this refinancing concentration through securing funds from alternative sources, implementing a "Medium Term Plan" encapsulating the Society's strategy to achieve those necessary aims to grow the business and ensuring that the Society's exposure to the TFS is relatively small in real terms (and represents a much smaller proportion when compared to other financial institutions who have drawn down under this scheme), there can be no assurance that such plans will be successful or that the Society will be able to refinance its obligations on satisfactory market terms. The Society's available funding options are regularly reviewed by the PRA. If such funding options are not successful in mitigating the impact of this refinancing concentration, the Society could face liquidity restraints. The Society manages its refinancing concentration under the government-backed liquidity schemes as part of its general ongoing financial requirements.

#### **The Society's hedging strategies may not prevent losses**

The Society is continually managing its exposure to interest rate and refinancing risks. If any of the variety of instruments and strategies the Society uses to hedge its exposure to these various types of risk is not effective, the Society may incur losses. The Society may not be able to obtain economically efficient hedging opportunities that will enable it to maintain its present hedging policies with respect to new assets and liabilities. Further, when a borrower defaults on a loan that is subject to a hedging arrangement, losses may be exacerbated as the Society is still required to meet the obligations of the derivative instrument.

#### **The Society's derivatives counterparties may not honour their contracts**

The Society uses derivatives to manage its market risks. These derivatives are negotiated with and transacted with a range of counterparties. While to date there has not been a situation in which any of the Society's derivative counterparties have not honoured their obligations under the relevant derivative agreement, a failure by one or more counterparties to honour the terms of its derivatives contract with the Society could have an adverse effect on the business, operations and financial condition of the Society. The Society is now centrally clearing all new eligible derivative contracts with third parties as required under Regulation (EU) 648/2012 (**EMIR**) following European Securities and Markets Authority (ESMA) rules. As required by EMIR, the Society's exposure is to a central counterparty clearing body, LCH Ltd. Margin management on an intra-day basis ensures any additional exposure due to mark to market changes in valuation is covered. Additionally, the Society has collateralised swap agreements in place with all major swap counterparties in order to minimise the risk of loss in the event of default by a counterparty. However, there can be no guarantee that such strategy will effectively prevent all counterparty-related loss.

#### **Market sentiment with respect to the Society, the financial services sector or the building society sector**

If sentiment towards banks, building societies and/or other financial institutions operating in the UK, including the Society, were to deteriorate, this may have a materially adverse impact on the Society. In addition, any such change in sentiment could result in an increase in the costs of, and a reduction in the availability of, wholesale market funding across the financial sector which could have a material

adverse effect on the liquidity and funding of all UK financial services institutions, including the Society.

Such deterioration in market sentiment could adversely affect the Society's liquidity and competitive position, particularly through cash outflows to meet collateral requirements on existing contracts. Confidence in the Society's business could be undermined, potentially increasing borrowing costs, limiting access to the capital markets and restricting the range of counterparties willing to enter into transactions with the Society.

The Society has experienced all of these effects in the past, although it is not possible to predict the precise effects of any future impact on sentiment.

**The Society's risk management may prove inadequate for the risks faced by its business and any failure to properly manage the risks which it faces could cause harm to the Society and its business prospects**

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.

The Society faces a wide range of risks in its business activities, including, in particular:

- 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, creditors 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 that assets and liabilities reprice at different times and / or by varying amounts, adversely affecting the net interest margin;
- 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; and

- 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.

The Society has a range of tools designed to measure and manage the various risks which it faces, see “*Part XIX: Risk Management*”.

### **Risks from the Society’s operations**

Operational risk and losses can result from a range of internal and external factors with the principal risk being a significant business continuity event. Internal factors include fraud, errors by employees, failure to document transactions properly or to obtain proper internal authorisation, failure to comply with regulatory requirements and conduct of business rules and equipment failures, particularly in relation to electronic banking applications. External factors include natural disasters, war, terrorist action or the failure of external systems, for example, those of the Society’s suppliers or counterparties.

Over recent years there has been a rapid rise in demand for digital products and services due to the convenience that they can bring. This has seen an influx of innovative new offerings in the market place and the number of challenger banks and Fintech companies has increased. Collectively the changes may pose a challenge to the Society’s core markets and product pricing, particularly if it is unable to introduce competitive products and services.

The Society has invested substantially in core systems to enable growth and make it easier for members to conduct business, and to provide operational efficiencies. Significant investment will be required in the future as the Society plans to update its core systems and enhance its digital presence. However, the scale and pace of these changes can lead to higher than planned investment costs and also create delivery challenges, potentially disrupting the Society’s operations and impacting the service experienced by customers.

Significant change programmes can also be difficult to manage in terms of costs and delivery schedule. Adverse variations in either costs to deliver or timing of delivery could have a material impact on the Society’s performance and profitability.

There is a risk that insurance arrangements do not sufficiently cover an event, requiring the Society to pick up the cost and adversely impacting profitability. The annual review of insurance arrangements is based on advice from brokers and an annual benchmarking exercise.

### **Market risks may adversely impact the Society’s business**

Market risk is the risk that the net value of, or net income arising from, the Society’s assets and liabilities is impacted as a result of market price or rate changes, specifically interest rates or equity prices. Changes in interest rate levels, yield curves and spreads may affect the interest rate margin realised between lending and borrowing costs.

There is a risk of a reduction in returns from the Society’s residential tracker mortgage assets whose rate is linked to the BoE Bank Rate with no floor should the BoE Bank Rate be reduced.

Falling house price measures (namely HPI) could lead to a reduction in the book value of West Bromwich Homes Limited properties.

The performance of financial markets may cause changes in the value of the Society’s investment and liquidity portfolios. Although the Society has implemented risk management methods designed to mitigate and control these and other market risks to which it is exposed and its exposures are constantly measured and monitored, there can be no assurance that these risk management methods will be effective, particularly in unusual or extreme market conditions. It is difficult to predict with accuracy

changes in economic or market conditions and to anticipate the effects that such changes could have on the Society's financial performance and business operations.

### **Information risk**

There is the risk that 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. As well as potential losses that would impact the Society it could also impact the Society's reputation. This could make customers, depositors and investors unwilling to do business with the Society, which could adversely affect its business, financial condition and results of operations and could damage its relationships with its regulators.

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. However, there can be no assurance that the Society's systems would not be susceptible to cyber attacks in all circumstances.

### **Reputational risk**

The Society's ability to attract and retain customers and conduct business with its counterparties could be adversely effected to the extent that the Society's reputation is damaged. Failure to address, or appearing to fail to address, various issues that could give rise to reputation risk could cause harm to the Society and the Society's business prospects. Reputational issues include, but are not limited to: appropriately addressing potential conflicts of interest; legal and regulatory requirements; ethical issues; adequacy of anti-money laundering processes; privacy issues; customer service issues; recordkeeping; sales and trading practices; proper identification of the legal, reputational, credit, liquidity and market risks inherent in products offered; and general business performance. A failure to address these issues appropriately could make customers unwilling to do business with the Society, which could adversely affect the Society's business, financial condition and results of operations.

### **Pension liability risk**

Risk arises from the Society's defined benefit pension scheme because the value of its asset portfolios and returns from them may be less than expected and because there may be greater than expected increases in the estimated value of the scheme's liabilities.

Increased longevity and/or poor investment returns could require the Society to contribute more to the scheme, which could be significant and have a negative impact on the Society's results of operations. The defined benefit scheme is closed to new members and existing members are no longer accruing service benefits. The assets of the pension funds are held and managed by a Trustee separate from the Society's assets. The Trustee takes extensive advice (actuarial, investment etc.) to minimise the impact of the risks identified.

### **Risks relating to the mis-selling of financial products**

There is currently significant regulatory scrutiny of the sales practices and reward structures that financial institutions have used when selling financial products. No assurance can be given that the Society will not incur liability for past, current or future actions, including failure to comply with applicable regulatory requirements, which are determined to have been inappropriate and any such liability incurred could be significant and materially adversely affect the Society's results of operations and financial position. In particular:

- certain aspects of the Society's business may be determined by the BoE, the PRA, the Financial Conduct Authority (the **FCA**), HM Treasury, the CMA, the Financial Ombudsman Service (the **FOS**) or the courts as not being conducted in accordance with applicable laws or regulations, or, in the case of the FOS, with what is fair and reasonable in the Ombudsman's opinion;
- the alleged mis-selling of financial products, including as a result of having sales practices and/or rewards structures that are deemed to have been inappropriate, may result in disciplinary action (including significant fines) or requirements to amend sales processes, withdraw products, or provide restitution to affected customers, all of which may require additional provisions to be recorded in the Society's financial statements and could adversely impact its future revenues from affected products; and
- the Society may be liable for damages to third parties harmed by the conduct of its business.

In addition, the Society faces both financial and reputational risk where legal or regulatory proceedings, or complaints before the FOS, or other complaints are brought against it or members of its industry generally in the English High Court or elsewhere. For example, in August 2010, the Financial Services Authority (the **FSA**) published a Policy Statement (**PS10/12**) on "The Assessment and Redress of Payment Protection Insurance Complaints" (the **Statement**). The Statement applies to all types of Payment Protection Insurance (**PPI**) policies and followed Consultation Paper (CP10/06). Following publication of the Statement, the British Bankers Association (**BBA**) and others requested a judicial review of the FSA's proposed approach to the assessment and redress of complaints in respect of sales of PPI. On 20 April 2011, the High Court ruled in favour of the FSA. The BBA chose not to appeal this ruling and the obligation for firms to comply with PS10/12 resulted in very significant provisions for customer redress made by several UK financial services providers.

In November 2014, the UK Supreme Court ruled in *Plevin v. Paragon Personal Finance Ltd* (**Plevin**) that a failure to disclose to a client a large commission payment on a single premium PPI policy made the relationship between a lender and the borrower unfair under section 140A of the Consumer Credit Act 1974 (the **CCA**). As a result and following an industry consultation, in March 2017 the FCA published final rules and guidance which may result in an increase in the volume of 'Plevin-based' unfair relationship claims brought against the lenders who failed to disclose significant PPI commissions when entering into credit agreements. A key aspect of the FCA's final rules is a PPI complaints deadline of 29 August 2019 for remaining PPI complaints to financial services firms or the FOS. There can be no assurance that the final rules and guidance will not result in further costs or requirements in relation to customer redress by institutions which have historically sold PPI.

#### **Changes in accounting policies or standards**

From time to time, the International Accounting Standards Board (the **IASB**) and/or the European Union change the international financial reporting standards (**IFRS**) issued by the IASB, as adopted by the European Commission (the **Commission**) for use in the European Union, that govern the preparation of the Society's financial statements. These changes could materially impact how the Society records and reports its financial condition and results of operations. In some cases, the Society could be required to apply a new or revised standard retroactively, resulting in restating prior period financial statements.

For example, IFRS 9: "*Financial Instruments*" is the new standard to replace IAS 39: "*Financial Instruments: Recognition and Measurement*". It will change the classification and measurement of some financial assets, the recognition and the financial impact of impairment and hedge accounting. IFRS 9 is required to be implemented in the Society's financial statements for the financial year ending 31 March 2019.

Amongst other changes, IFRS 9 is replacing the incurred loss approach to impairment of IAS 39 with one based on expected credit losses (**ECL**), which will result in earlier recognition of credit losses. This introduces a number of new concepts and changes to the approach to provisioning compared with the methodology under IAS 39.

The European authorities have recognised the risk that application of IFRS 9 may lead to a sudden significant increase in ECL provisions and consequently a sudden decrease in the capital ratios of institutions. Accordingly, the European authorities have passed Regulation (EU) 2017/2395 (the **CRR IFRS 9 Regulation**) introducing transitional periods for mitigating the impact of the introduction of IFRS 9 on own funds.

Under the CRR IFRS 9 Regulation, it is proposed that where an institution's opening balance sheet after adoption of IFRS 9 reflects a decrease in Common Equity Tier 1 (**CET1**) capital as a result of increased ECL provisions (net of tax effect) compared to the previous closing balance sheet, the institution should be allowed to include in its CET1 capital a portion of the increased provisions during a transitional period. This transitional period should have a maximum duration of five years as from the opening balance sheet date in 2018 (in the case of the Society, 1 April 2018) and the portion of ECL provisions that can be included in CET1 capital should decrease over time down to zero to deliver full implementation by the end of the five year period. As provisions incurred after implementation could rise significantly and unexpectedly due to a worsening macroeconomic outlook, the CRR IFRS 9 Regulation also provides that institutions should be given additional relief in such cases through the transitional arrangements.

The Society's IFRS 9 implementation project is progressing to timetable, with a number of updates made to the Society's systems and business processes. New models, built to meet the ECL requirements defined in the standard, have been tested and will be subject to parallel running during the second half of the 2017/18 financial year with supporting governance created to ensure that the models and integral assumptions are properly controlled. The financial impact of implementing IFRS 9 is highly dependent on the portfolios and economic view as at the date of transition. Further details on IFRS 9 can be found on pages 55 to 56 of the 2017 Financial Statements.

The IASB may make other changes to financial accounting and reporting standards that govern the preparation of the Society's financial statements, which the Society may adopt prior to the date on which such changes become mandatory if determined to be appropriate by the Society, or which the Society may be required to adopt. Any such change in the Society's accounting policies or accounting standards could materially affect its reported financial condition and results of operations.

## **Taxation**

The Society's activities are principally conducted in the UK and it is therefore subject to a range of UK taxes at various rates. Future actions by the Government to increase tax rates or to impose additional taxes would reduce the Society's profitability. Revisions to tax legislation or to its interpretation might also affect the Society's financial condition in the future. Any such assessments could be material which might also affect the Society's financial condition in the future.

The Society holds a deferred tax asset on its balance sheet, predominantly arising from losses incurred over the period 2008/9 to 2012/13. During the 2016/17 financial 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 Society's tax charge by reducing the Society's forecast profitability and thereby 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 £6.0 million has been recorded to write down the value of the brought forward deferred tax asset to a level which the Society deems recoverable in the next five years, based upon the detailed forecasts included within the Group's Medium Term Plan.

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. 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 ECL and increases in the BoE Bank Rate of interest represent the most subjective areas of judgement in management's projections of future taxable profits. The Society'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. There is a risk that these projections are incorrect and the Society's tax position could be affected.

## 2. REGULATORY RISKS

The Society is regulated by the FCA and the PRA which regulate, amongst other things, the sale of residential mortgages, consumer lending, investment advice and general insurance products. The regulatory regime requires the Society to be compliant across many aspects of activity, including the training, authorisation and supervision of personnel, systems, processes and documentation. If the Society fails to be compliant with relevant regulations, there is a risk of an adverse impact on the business due to sanctions, fines or other action imposed by the regulatory authorities. Customers may also have a right of redress under section 138D of FSMA for breach of an FCA or PRA rule. This is particularly the case in the current market environment, which is witnessing increased levels of government intervention in the banking, personal finance and real estate sectors.

Future changes in regulation, fiscal or other policies are unpredictable and beyond the Society's control and could materially adversely affect its business or operations. Future legislative and regulatory changes could force the Society to comply with certain operational restrictions, take steps to raise further capital, and/or increase the Society's expenses and/or otherwise adversely affect the Society's business results, financial condition or prospects. Minimum regulatory requirements may increase in the future and/or the FCA or the PRA may change the manner in which they apply existing regulatory requirements. The FCA, PRA, and other bodies such as the FOS, could impose further regulations or obligations in relation to current and past dealing with retail customers. As a result, the Society may incur costs in complying with these regulations or obligations relating to its business, including potential compensation and costs relating to sales advice given to retail customers. Regulators and other bodies in the UK and the EU have produced a range of proposals for future legislative and regulatory changes which could impose operational restrictions on the Society, requiring it to raise further capital, increase its expenses and/or otherwise adversely affect its business results, financial condition or prospects.

These include, among others:

- Changes to the Markets in Financial Instruments Directive (**MiFID**) and its various implementing measures, which together regulate the provision of investment services and activities in relation to a range of areas, including client classification, conflicts of interest, client order handling, investment research and financial analysis, suitability and appropriateness, transparency obligations and transaction reporting. MiFID has largely been replaced by a revised directive, MiFID II, and a new regulation (Markets in Financial Instruments Regulation or **MiFIR**), which entered into force on 2 July 2014. The changes to MiFID include expanded supervisory powers that include the ability to ban specific products, services or practices. The majority of the provisions of MiFID II and MiFIR and the implementing laws and regulations were required to be implemented by 3 January 2018;



- The General Data Protection Regulation (**GDPR**) comes into force in May 2018 and applies to personal data. Its definition is more detailed than the Data Protection Act (**DPA**) and makes it clear that information such as an online identifier (for example, an IP address) can be personal data. It applies to both automated personal data and to manual filing systems where personal data is accessible according to specific criteria. This is wider than the DPA's definition and could include chronologically ordered sets of manual records containing personal data. A significant programme of work is in place to make the changes necessary to meet the requirements. In addition, the Society has a deadline of 31 December 2018 to comply with the Basel Committee on Banking Supervision's regulation number 239 entitled "*Principles for effective risk data aggregation and risk reporting*", which aims to strengthen risk data aggregation capabilities and internal risk reporting practices; and
- The Payment Services Regulations 2017 brought PSD2 into UK law, with effect from 13 January 2018. Key changes include the addition of account information services (**AIS**) and payment initiation services (**PIS**) as regulated payment services, new security requirements and increased focus on consumer protection. There are also changes to the scope of the conduct of business rules and the list of exemptions.

At this point it is difficult to predict the effect that any of these changes will have on the Society's operations, business and prospects or how any of the proposals discussed above will be implemented in light of the fundamental changes to the regulatory environment proposed by the Government and/or the European Commission. Depending on the specific nature of the requirements and how they are enforced, the changes could have a significant impact on the Society's operations, structure, costs and/or capital requirements. Accordingly, the Society cannot assure investors that the implementation of any of the foregoing matters will not have a material adverse effect on its operations, business, results, financial condition or prospects.

Furthermore, the Society cannot assure investors that any other regulatory or legislative changes or any other Governmental interventions that may be proposed or which may materialise in the future will not have a material adverse effect on its operations, business, results, financial condition or prospects. Whilst the scope and nature of any such future changes are unpredictable, any interventions or regulations designed to increase the protections for UK retail and other customers of banks and building societies, for example through stricter regulation on repossessions and forbearance by mortgage lenders, could materially adversely affect the Society's business or operations.

The Society is also subject to a number of EU and UK proposals and measures targeted at preventing financial crime (including anti-money laundering and terrorist financing). This includes the EU's Fourth Anti-Money Laundering Directive, which was required to be implemented in Member States by June 2017 and aims to enhance processes to counter money laundering and terrorist financing. The Society is committed to operating a business that prevents, deters and detects money laundering and terrorist financing, and will introduce any changes required in line with the new directive and industry guidance. However, if there are breaches of these measures or existing law and regulation relating to financial crime, the Society could face significant administrative, regulatory and criminal sanctions as well as reputational damage which may have a material adverse effect on the Society's operations, financial condition and prospects.

The Society is also investing significantly to ensure that it will be able to comply with developing regulatory requirements and emerging consumer trends and preferences for digital services. If the Society is unsuccessful in efficiently adopting the requisite new compliance practices, this will adversely impact its ability to operate in the financial services markets and to deliver an appropriate level of operational and financial performance.

#### **Implementation of and/or changes to the Basel Framework**

The Basel Committee on Banking Supervision (the **Basel Committee**) approved significant changes to Basel II (being the revised international capital framework of the Basel Committee, published in 2004) regulatory capital and liquidity framework in 2011 (such changes being commonly referred to as **Basel III**). In particular, Basel III provides for a substantial strengthening of existing prudential rules, including requirements intended to reinforce capital requirements (with heightened requirements for global systemically important banks) and to establish a leverage ratio "backstop" for financial institutions and certain minimum liquidity ratios (the LCR and the NSFR). In the EU the LCR has applied since 1 October 2015. The LCR measures whether firms hold an adequate level of "high-quality liquid assets" against net cash outflows arising in a 30 day stress scenario period. As of 1 January 2018, the minimum LCR is required to be 100 per cent. Under Basel III, the NSFR, which measures the amount of "stable funding" (i.e. reliable sources of funds over a one year period under conditions of stress), was intended to be implemented as a binding standard from January 2018, but it is not yet a binding standard in the EU.

Until recently, certain aspects of Basel III remained subject to further agreement. However, the outstanding post-crisis regulatory reforms were endorsed by the Group of Central Bank Governors and Heads of Supervision (**GHOS**), the Basel Committee's oversight body, on 7 December 2017. The revised standards are intended to take effect from 1 January 2022 and will be phased in over five years. The GHOS also endorsed the Basel Committee's proposal to extend the implementation date of the revised minimum capital requirements for market risk, which were originally set to be implemented in 2019, to 1 January 2022 (which will constitute both the implementation and regulatory reporting date for the revised framework). Implementation of the Basel framework (to the extent that it has not already been fully implemented in member countries) and/or of any of the changes put forward by the Basel Committee as described above may have an impact on the capital requirements in respect of the Society.

The Basel Committee has also separately published certain proposed revisions to the securitisation framework, including proposed new hierarchies of approaches to calculating risk weights and a new risk weight floor of 15 per cent.

The Basel III reforms have been implemented in the EEA through the Capital Requirements Regulation and the Capital Requirements Directive (together **CRD IV**). CRD IV became effective in the UK and other EU member states on 1 January 2014. CRD IV permits a transitional period for certain of the enhanced capital requirements and certain other measures which are not expected to be fully implemented until 2019. On 23 November 2016 the European Commission published an extensive package of reforms to prudential standards proposing amendments to the framework applicable to financial groups. The reforms (the **Banking Reform Package**) predominantly amend CRD IV and the EU's Bank Recovery and Resolution Directive (2014/59/EU) (the **BRRD**). Among other things, the Banking Reform Package seeks to bring the EU's existing Minimum Requirement for Own Funds and Eligible Liabilities (**MREL**) under the BRRD in line with the Financial Stability Board's Total Loss-Absorbing Capacity standard for global systemically important institutions. The Banking Reform Package includes a directive, published in the Official Journal on 27 December 2017 (the **Insolvency Hierarchy Directive**), which amends the BRRD and is required to be implemented in the UK by 29 December 2018, harmonising the creditor hierarchy of EU banks and creating an MREL-eligible non-capital debt instrument, the features of which are also set out in the Insolvency Hierarchy Directive. This is intended to bring increased flexibility for future MREL issuance. The directive's implementation in the UK is subject to further legislation, the effect of which is as yet undetermined.

CRD IV has also introduced the simpler non-risk based leverage ratio as a supplementary measure. The leverage ratio is calculated as Tier 1 capital divided by total leverage ratio exposure (total exposure being the sum of on-balance sheet exposures, derivative exposures, securities financing transaction exposures and off-balance sheet items). The proposed amendments to the CRR in the Banking Reform Package provide for an EU-wide leverage ratio minimum requirement of 3 per cent. to be implemented as a binding measure in 2018 in accordance with the CRD IV. In October 2017 the PRA published a

policy statement increasing the minimum leverage ratio requirement from 3% to 3.25% of total exposures.

In general, investors should consult their own advisers as to the regulatory capital requirements applicable in respect of their holdings of the Securities, if any, and as to the consequences for and effect on them of any changes to the Basel framework (including the changes described above) and the relevant implementing measures. No predictions can be made as to the precise effects of such matters on any investor or otherwise.

### **Risks relating to the Banking Act 2009 and the BRRD**

The Banking Act 2009 (the **Banking Act**) includes provision for a special resolution regime pursuant to which specified UK authorities, HM Treasury, the PRA, the FCA and the Bank of England (together, the **Authorities**) have extended tools to deal with the failure (or likely failure) of a UK bank or building society. In addition, powers may be used in certain circumstances in respect of UK established banking group companies, where such companies are in the same group as a relevant UK or third country institution or in the same group as an EEA credit institution or investment firm.

The tools available under the Banking Act include share and property transfer powers (including powers for partial property transfers), bail-in powers, certain ancillary powers (including powers to modify certain contractual arrangements in certain circumstances) and special insolvency procedures which may be commenced by the UK authorities. It is possible that the extended tools described above could be used prior to the point at which an application for insolvency proceedings with respect to a relevant entity could be made. Further, the Authorities have a wide discretion in exercising their powers under the special resolution regime, including modifying or setting aside any Act of Parliament by order of HM Treasury to facilitate its Banking Act objectives.

In general, the Banking Act requires the UK authorities to have regard to specified objectives in exercising the powers provided for by the Banking Act. One of the objectives (which is required to be balanced as appropriate with the other specified objectives) refers to the protection and enhancement of the stability of the financial system of the UK. The Banking Act includes provisions related to compensation in respect of transfer instruments and orders made under it. In general, there is considerable uncertainty about the scope of the powers afforded to the UK authorities under the Banking Act and how the authorities may choose to exercise them.

If an instrument or order were to be made under the Banking Act in respect of a relevant entity, such instrument or order may (amongst other things) affect the ability of such entity to satisfy its obligations under the Transaction Documents and/or result in modifications to such documents. In particular, modifications may be made pursuant to powers permitting certain trust arrangements to be removed or modified and/or via powers which permit provision to be included in an instrument or order such that the relevant instrument or order (and certain related events) is required to be disregarded in determining whether certain widely defined "default events" have occurred (which events would include certain trigger events included in the Transaction Documents in respect of the relevant entity, including termination and acceleration events). As a result, the making of an instrument or order in respect of a relevant entity may affect the ability of the Society to meet its obligations. While there is provision for compensation in certain circumstances under the Banking Act, there can be no assurance that investors would recover compensation promptly and equal to any loss actually incurred.

This regime has also been amended to ensure that it is compliant with the BRRD. The BRRD was published in the Official Journal of the EU on 12 June 2014 and generally came into force on 2 July 2014 (with Member States required to implement it by 31 December 2014). Amongst other things, the BRRD provides for the introduction of a package of minimum early intervention and resolution-related tools and powers for relevant authorities (including a bail-in tool) and for special rules for cross-border groups. The BRRD has been implemented in the UK via the Bank Recovery and Resolution Order

2014 (**BRRD Order**), which came into force on 1 January 2015. The BRRD has been supplemented by delegated regulations setting out further standards relating to the resolution framework.

There can be no assurance that the Society will not be adversely affected by the amendments and/or any action taken under the bail-in tool. Accordingly, it is not yet possible to assess the full impact of the UK bail-in tool on a relevant entity and there can be no assurance that it will not materially and adversely affect the relevant entity's operating results, financial position and prospects.

At present, the Authorities have not made an instrument or order under the Banking Act or the BRRD Order in respect of the relevant entities referred to above and there has been no indication that they will make any such instrument or order, but there can be no assurance that this will not change and/or that the Society will not be adversely affected by any such instrument or order if made.

Although the Banking Act provides for conditions to the exercise of any resolution powers and the European Banking Authority (**EBA**) has published guidelines setting out the objective elements for determining whether an institution is failing or likely to fail, it is uncertain how the Authorities would assess such conditions in any particular situation. The relevant Authorities are also not required to provide any advance notice of their decision to exercise any resolution power. Therefore, holders of Securities may not be able to anticipate a potential exercise of any such powers nor the potential effect of any exercise of such powers on the Society or the Securities.

### **Risks relating to regulatory capital and liquidity requirements**

The Society is subject to regulatory capital and liquidity requirements that could have an impact on its operations. Changes to the regulatory capital and liquidity requirements under which the Society operates could hinder growth by prescribing more stringent requirements than those with which it currently complies. UK regulators and international policymakers are reviewing a number of areas of the regulatory capital framework, with a view to making changes as appropriate. These areas include a MREL, capital requirements for residential mortgages and review of the standardised approach for risk and IRB model framework. The MREL currently places no obligation on the Society to hold additional capital.

Currently, the Society applies the Standardised Approach, and the Basel III reforms to the Standardised Approach proposed for implementation in 2022 represent a significant revision to earlier proposals. These proposals are not expected to have a significant impact on traditional building societies. The Society is making significant progress on its regulatory project to move to the Internal Ratings Based (**IRB**) approach to calculating its capital requirements for credit risk, which commenced in October 2015. Reform proposals affecting IRB are still under review and it is not clear what the final impact will be. The Society would expect to see a capital benefit from adopting an IRB approach but due to the uncertainty this is difficult to assess. In September 2017, following a review of the progress made to date on the IRB project the Board re-affirmed its commitment to the continued investment on the project, which is considered to provide significant benefits in terms of credit risk management in addition to the potential for a reduction in capital requirements, and is indicatively targeting a submission of its application for IRB permission to the PRA in 2018. Due to the low credit risk nature of the Society's core residential mortgage books, the Society believes that IRB should ultimately improve the Society's capital position. However any substantial changes to the regime could result in further increases in the level of capital which the Society is required to hold and could incur additional costs in order to ensure implementation of, and continued compliance with, the evolving prudential regime.

### **Financial Services Compensation Scheme**

The FSMA established the Financial Services Compensation Scheme (the **FSCS**), which pays compensation to eligible customers of authorised financial services firms which are unable, or likely to be unable, to pay claims against them. An institution's FSCS levy is linked to its share of the relevant

UK market (for example, the deposit protection levy is linked to the share of protected deposits). The FSCS levy may have a material impact on the corporate profits of the Society. As at the time of these Listing Particulars, a number of claims against the FSCS have been triggered. Claims on the FSCS are funded by loans from the BoE, and until such loans are repaid, increased levies on UK deposit-taking institutions fund interest payments on such loans. The provision of £0.8 million 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.

### 3. RISKS RELATED TO THE CCDS

*Capitalised terms used and not otherwise defined in this section 3 (Risks related to the CCDS) have the meaning given to them in "Part IX: Conditions of Issue of the Core Capital Deferred Shares" of these Listing Particulars.*

#### **CCDS are a financial instrument with complex features**

CCDS have been designed for building societies (which do not have ordinary share capital) to allow them to raise Common Equity Tier 1 capital. Certain key features of the CCDS are as follows:

- CCDS are perpetual instruments. Holders of CCDS have no right to have their CCDS redeemed and the Society has no obligation or right to redeem the CCDS at any time;
- CCDS holders have no right to any Distributions on the CCDS (or to any particular level or frequency of payment of such Distributions, if paid), the declaration of which by the Board is wholly discretionary and may be restricted by applicable law and regulation. The Rules of the Society provide for an upper limit on the amount of Distributions which the Society is permitted to declare on each CCDS in respect of any financial year;
- the rights of CCDS holders to participate in the winding-up or dissolution of the Society are limited to (i) a deeply subordinated claim in respect of any declared, unconditional and unpaid Distributions (if any) on the CCDS at the time of the winding-up or dissolution, and (ii) a capped entitlement to share in surplus assets (if any) remaining in the Society after all depositors and creditors (including subordinated creditors) of the Society have been repaid in full;
- investors in CCDS will have no member voting rights at general meetings of the Society in respect of their CCDS whilst the CCDS are held through the Clearing Systems, and even if (which the Directors consider unlikely) CCDS in definitive form are issued and held directly by investors outside the Clearing Systems, their member voting rights at general meetings of the Society will be insignificant; and
- CCDS holders may have their holdings diluted by an issuance of additional CCDS by the Society. There are no pre-emption rights in respect of the CCDS.

As a provider of core capital to the Society, an investor in CCDS should be prepared to suffer losses on its investment if, in particular, the Society and/or the financial sector generally approaches or enters into a period of financial stress. Such losses could be manifested in a number of ways, including (without limitation):

- if the Society elects or is required to cease declaring Distributions (or to reduce the amount declared);
- if the market price of the CCDS falls significantly;

- if further CCDS or other instruments are issued which dilute (either initially or upon conversion into CCDS) the holdings of CCDS investors; and
- if, in a worst-case scenario, the UK authorities take action under the Banking Act 2009 (or similar future legislation) or the Society enters into an insolvent winding-up.

**The CCDS are deeply subordinated instruments and holders of the CCDS will be entitled to only a limited share in any surplus assets of the Society on a winding-up of the Society**

The CCDS do not constitute a debt or a liability of the Society, and are the most junior-ranking investment in the Society. As a result, in the event of an insolvent winding-up or dissolution of the Society, an investor in CCDS will lose the entire amount of its investment and, even on a solvent winding-up or dissolution, an investor may recover none or only some of its investment.

The rights and limitations on the rights of an investor in CCDS on a winding-up or dissolution of the Society are as follows:

- ***Lowest ranking claim:*** the claims of holders in respect of their CCDS will rank behind the claims of all depositors, creditors of the Society, including subordinated creditors (such as the holders of Tier 2 Notes) and holders of other deferred shares (including permanent interest bearing shares) in the Society. Accordingly, CCDS holders will not be entitled to receive any amounts in the winding-up or dissolution of the Society unless all depositors and creditors (including subordinated creditors) and other holders of deferred shares (including permanent interest bearing shares) in the Society are first paid in full;
- ***Subordinated claim for declared but unpaid Distributions:*** If, at the time of commencement of winding-up or dissolution, the Society has declared but not yet paid a Distribution, then (provided the Distribution is unconditional, or that any conditions stated to apply to the Distribution are fulfilled prior to commencement of winding-up or dissolution) holders will be entitled to claim for such Distribution. However, that claim will be deeply subordinated, and will rank behind the claims of all creditors (including subordinated creditors) of the Society;
- ***No other fixed claims:*** Save for the claim (if any) in respect of a declared but unpaid Distribution, CCDS holders will not have a fixed claim in such winding-up or dissolution for the amount of their initial investment in CCDS (or for any other amount);
- ***Right to a proportionate and capped share in any Surplus:*** CCDS holders will be entitled only to share in the surplus assets (if any) of the Society remaining following payment in full of the claims of all depositors and creditors (including subordinated creditors) of the Society (and, if applicable, after payment of the claim in respect of declared but unpaid Distributions), any such surplus assets being a **Surplus**. Any Surplus would be shared between the CCDS holders and other qualifying members of the Society on a proportionate basis. However, in the case of CCDS holders, the proportionate amount payable to them is subject to a cap, which may be less than an investor's initial investment in the CCDS even if there is ample Surplus available for distribution in the winding-up or dissolution. The CCDS Conditions contain provisions for determining the proportionate amount of Surplus which would be available for distribution amongst holders of the CCDS and the determination of the capped amount of Surplus which would be distributed per CCDS. Investors should also note that further issues of CCDS may have a dilutive effect on the amount which an investor would be eligible to receive on a winding-up or dissolution of the Society. See "*The Society is entitled, without the consent of the holders of the CCDS, to issue additional CCDS and other instruments ranking in priority to the CCDS at any time. Any such additional issue of CCDS and/or such other instruments may have a dilutive effect on existing CCDS*" below; and

- ***No right of set off:*** Holders of CCDS are not entitled, on any account, to set-off any amounts owing to them in respect of their CCDS against amounts owing by them to the Society.

The above factors mean that an investor in CCDS will lose its entire investment on an insolvent winding-up or dissolution of the Society and, even on a solvent winding-up or dissolution, an investor may recover none or only some of its investment.

Furthermore, the ranking of CCDS in a winding up can also be expected to have a direct impact on the relative losses imposed on holders of CCDS in a resolution of the Society or a capital write-down under the Banking Act, as such resolution and capital write-down powers ought to be used in a manner that respects the hierarchy of claims in an ordinary insolvency - see *“The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK deposit-taking institutions which are considered to be at risk of failing. The exercise of any of these actions in relation to the Society and/or the CCDS and/or Tier 2 Notes could materially adversely affect the value of any Securities and the rights of the holders thereof”*.

**CCDS are perpetual instruments and the Society has no obligation nor any right to redeem the CCDS. In addition, whilst an established secondary trading market for CCDS may develop, it may not be or remain liquid. As a result, an investor in CCDS should be prepared to hold its CCDS for an indefinite period of time**

The CCDS constitute permanent non-withdrawable deferred shares (as defined in the Act) in the Society and have no maturity date. The Society has neither an obligation nor any right to redeem or, subject to limited exceptions related to purchases of CCDS, cancel the CCDS at any time and CCDS holders do not have any right to require the Society to redeem, purchase or cancel the CCDS. Any CCDS holder wishing to exit its investment would need to seek to sell its CCDS in the secondary market.

Whilst the Society intends to apply to the Luxembourg Stock Exchange for the CCDS to be admitted to the Official List of the Luxembourg Stock Exchange and to listing on the Euro MTF, there can be no assurance that a secondary market in the CCDS will be established and, if any such market is established, it may be illiquid and prices may be volatile. The market price of the CCDS will also be affected by many factors, including the actual or perceived ability of the Society to pay Distributions in respect of the CCDS. Accordingly, even if a holder is able to sell CCDS in a secondary market, there can be no assurance that the price of such sale would enable the investor to recover its initial investment, and the investor may suffer significant losses on its investment if the market price is lower than the price at which such investor acquires CCDS. Investors in the CCDS should be prepared to hold their CCDS indefinitely.

Even if an established secondary market for CCDS develops, there can be no assurance that such market will be or remain liquid, and such market may be more volatile than for more conventional investments with a developed secondary market. The CCDS contain features which may not align directly to the investment criteria of fixed income investors or traditional equity investors, including investors that have previously invested in mutual regulatory capital. Market prices (to the extent quoted) for the CCDS can go down as well as up, depending upon a number of factors including (without limitation) the actual or perceived financial condition of the Society and prevailing market conditions generally from time to time. Given the Society’s proposed distribution policy with respect to the CCDS (as set out in *“Part V – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy – 3. Distribution Policy in respect of the CCDS”* of these Listing Particulars), the Society anticipates that any trading in the CCDS is likely initially to be at a substantial discount to the issue price of £100 per CCDS. There can be no assurance that an investor will be able to sell its CCDS at a price equal to or higher than the price at which it purchased such CCDS, and the price which an investor achieves upon selling its CCDS could be considerably lower than the price at which it purchased such CCDS. See *“The trading price of the Securities may fluctuate which could lead to investors losing some or all of their investment”* below.

As a result of the absence of redemption rights or obligations in the terms of the CCDS and the uncertainties regarding secondary market trading in the CCDS, an investor in CCDS should be prepared to hold its CCDS for an indefinite period of time.

**The declaration of Distributions by the Board is wholly discretionary and therefore investors in the CCDS cannot be assured of a regular (or any) return on their investment. In addition, the amount of any Distribution paid on the CCDS is entirely within the discretion of the Board and subject to a cap and other limitations**

The declaration of any Distributions from time to time by the Board is wholly discretionary at all times, and may be restricted by applicable law and regulation. Irrespective of any mandatory restrictions on the Society's ability to declare Distributions from time to time, the Society does not currently anticipate paying any Distributions in respect of the CCDS in respect of the financial years ended 31 March 2018 and 31 March 2019, and any Distributions thereafter will be subject to, amongst other things, the Society's financial performance and the discretion of the Board. See "*Part V – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy – 3. Distribution Policy in respect of the CCDS*" below.

With respect to any given financial year of the Society, the Board may declare an interim Distribution (an **Interim Distribution**) during such financial year and/or a final Distribution (a **Final Distribution**) in respect of such financial year. Interim Distributions and Final Distributions are independent, and accordingly whether or not the Board declares an Interim Distribution during any financial year shall have no effect or bearing on the Board's discretion whether or not to declare a Final Distribution in respect of that financial year (save that the amount of the Final Distribution (if any) declared in respect of a financial year shall not, when aggregated with any Interim Distribution paid in respect of that financial year, exceed the Cap referred to below). If at any time the Board elects to declare any Interim Distribution or Final Distribution, the amount of such Distribution will also be entirely within the discretion of the Board, subject to the restrictions on the maximum amount of any Distribution described below.

The Society's distribution policy in respect of the CCDS may set out an indication of the level of Distributions which the Board expects to declare on the CCDS. Any such indication shall not be binding on the Board or the Society, and an election by the Board not to declare a Distribution (whether an Interim Distribution or a Final Distribution) in line with any stated expectation (or at all) shall not constitute a default under the CCDS or for any purpose. The Society will be entitled to amend the distribution policy at any time, in which case the Society will promptly publish the revised policy on its website.

The Society does not currently anticipate paying any Distributions in respect of the CCDS in respect of the financial years ended 31 March 2018 and 31 March 2019. Thereafter, the Society intends to grow its Distributions on the CCDS from £1.00 per CCDS for the year ended 31 March 2020 up to £4.50 per CCDS in respect of the year ended 31 March 2023, and thereafter to adopt a stable distribution policy at that level. However, there can be no assurance that the Society will make any such Distributions, or that the Board will not revise its distribution policy. The declaration and payment of Distributions is entirely at the Board's discretion, and the Society's ability or willingness to declare Distributions will depend upon a range of factors, including (but not limited to) the Society's profitability, availability of distributable resources, business outlook, capital and liquidity and the appropriate rewarding of CCDS holders, as well as the duty of the Board to act in the best interest of the Society and to have regard to the interests of all categories of the Society's members (of which CCDS holders form only one such category). See "*Part V – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy - 3. Distribution Policy in respect of the CCDS*" below.

If at any time the Board elects not to declare any Interim Distribution or Final Distribution, no Distribution or other amount in respect of the relevant period shall accumulate to CCDS holders or be payable at any time thereafter, and CCDS holders shall have no right to any Distribution or other amount in respect of such period.



Further, Distributions may be declared that are, in whole or in part, subject to the satisfaction of one or more conditions. In such circumstances, if any such condition is not satisfied on or prior to the scheduled date for payment, such Distribution (or, if applicable, the relevant part of such Distribution) shall not accumulate to CCDS holders or be payable at any time thereafter.

Neither an election by the Board not to declare any Interim Distribution or Final Distribution, nor non-payment of any Distribution (or any part thereof) in respect of which a relevant condition to payment has not been satisfied on or before the scheduled payment date, shall constitute a default by the Society under the CCDS for any purpose, and neither event shall entitle CCDS holders to petition for the winding-up or dissolution of the Society.

Distributions can be paid only out of the aggregate of profits and reserves (if any) of the Society which are available, in accordance with applicable law and regulation for the time being, for the payment of such Distribution (**Distributable Items**). The Society is not permitted to, and will not, declare a Distribution that is greater than the amount of Distributable Items available for payment of such Distribution. Changes to applicable law and regulation, including changes to the Act, could potentially have an impact on what items the Society may use for the purpose of paying Distributions.

Further, CRD IV requires the Society to maintain additional capital buffers which may be varied by the PRA or the FPC from time to time comprising CET 1 capital on top of the minimum capital requirements. Pursuant to Article 141 of CRD IV, the Society will not be permitted to declare Distributions or certain other discretionary payments (such as discretionary employee bonuses), to the extent that such payments would decrease its CET1 capital to a level where the combined buffer requirement is not met in full and, if at any point the Society fails to maintain sufficient CET1 capital to meet the combined buffer requirement, it will not be permitted to pay any Distributions in excess of a 'maximum distributable amount' (**MDA**) calculated in accordance with Article 141. The CET1 capital used to satisfy the combined buffer requirement cannot also be used to satisfy the Society's minimum capital requirement, Pillar 2A additional individual capital requirement or MREL requirement, each of which must be met in full before CET1 capital can be applied to meeting the combined buffer requirement. Accordingly, to the extent that any increases in the Society's Pillar 2A or MREL requirements are, or are required to be, met with CET1 capital, the amount of CET1 capital available to meet the combined buffer requirement may be reduced. The Society's capital requirements (including individual guidance or, under CRD IV, Pillar 2A requirements) are, by their nature, calculated by reference to a number of factors, any one of which or combination of which may not be easily observable or capable of calculation by investors. Investors may not be able to predict accurately the proximity of the risk of distributions being prohibited from time to time as a result of the operation of Article 141 of CRD IV.

For present capital planning purposes, upon successful conclusion of the liability management exercise announced by the Society on 13 December 2017 (the **LME**) and assuming only those PIBS holders from whom binding commitments have been received by the Society participate in the LME, the Society is currently anticipating an end-state CET1 capital requirement indicatively equivalent to 13.7 per cent. of RWAs as at 30 September 2017. As at 30 September 2017 the Society had a CET1 ratio of 14.1 per cent. The capital framework does not provide any automatic MDA restriction on a leverage basis.

In addition, the total Distribution declared on each CCDS in respect of any given financial year of the Society (being the aggregate of the Interim Distribution (if any) and the Final Distribution (if any) declared in respect of such financial year) must not exceed the prevailing periodic distributions cap (the **Cap**) determined in accordance with the Rules. The Rules provide that the initial Cap, which would have been applicable to Distributions in respect of the financial year to 31 March 2015 had CCDS been in issue during that financial year, was £15 per CCDS, and that (subject as stated below) in respect of each subsequent financial year the Cap will be adjusted for inflation (which, for the avoidance of doubt, would include negative inflation) by reference to the United Kingdom Consumer Price Index (CPI) (or any successor to that index). Such adjustment will be made by applying the CPI annual

inflation percentage published by the Office for National Statistics in its statistical bulletin for the last full calendar month of the financial year in respect of which the Distributions are payable (being the percentage increase or decrease over the twelve months to and including that month) to the prevailing Cap.

The prevailing Cap in respect of the financial year to 31 March 2017 was £15.42. For illustrative purposes only (as the Board is not intending to declare any Distributions in respect of the Society's financial year to 31 March 2018), the Cap on Distributions for the financial year to 31 March 2018 will be determined by applying the CPI annual inflation percentage published by the Office for National Statistics in its statistical bulletin for March 2018 to the prevailing Cap in respect of the financial year to 31 March 2017 of £15.42.

If at any time the adjustment of the Cap in the manner described above would prejudice the regulatory capital treatment of the CCDS, the Society will disapply those adjustment provisions and the Cap will revert to £15 per CCDS.

Prospective investors should note that the Cap represents the maximum permitted Distribution in respect of a financial year which the Board could elect to declare, and (as stated at Rule 27(2) of the Society's Rules) is designed to protect the reserves of the Society. It is not a target or any other indication of the Board's intentions as regards the declaration of Distributions. For the Board's initial distribution policy in respect of the CCDS, see "*Part V – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy - 3. Distribution Policy in respect of the CCDS*" below.

Notwithstanding the availability of sufficient Distributable Items, the Board will not declare any Distribution if the PRA requires the Society to refrain from making any Distributions on the CCDS at any time or whilst any specified circumstances subsist or during a specified period.

As a result of the above factors, investors in the CCDS may not receive a regular, or any, return on their investment in CCDS. In addition, if the Board elects not to declare a Distribution in respect of any given financial year, or any Distribution declared is lower than market expectations, or if the Society alters its Distribution Policy to reduce the target level of Distributions on the CCDS, this will be likely to have an adverse effect on the market price of the CCDS.

### **No gross-up obligation**

On the basis of UK tax law and practice prevailing as at the date of these Listing Particulars, all payments of Distributions in respect of the CCDS are expected to be made without withholding or deduction for or on account of any present or future taxes or duties of whatever nature imposed or levied by or on behalf of the UK or any political subdivision or any authority thereof or therein having power to tax.

However, if any payments under or in respect of the CCDS were to become subject to any withholding or deduction for or on account of any taxes, the Society has no obligation to pay an additional amounts in respect thereof. Accordingly, the CCDS holders would only be entitled to receive the net amount of the relevant payment following such deduction or withholding, the payment of such net amount would discharge the Society's obligations in respect of the relevant payment in full, and the market price of the CCDS (if any) may be adversely affected.

**The Society is entitled, without the consent of the holders of the CCDS, to issue additional CCDS and other instruments ranking in priority to the CCDS at any time. Any such additional issue of CCDS and/or such other instruments may have a dilutive effect on existing CCDS**

The Society is entitled, without the consent or approval of the CCDS holders, to issue additional CCDS that are consolidated and form a single series with the CCDS (**Additional CCDS**) and also to issue other instruments ranking in priority to the CCDS. Such instruments may include instruments

convertible into or exchangeable for CCDS, such as instruments which, in a stress scenario, are convertible into or exchangeable for CCDS automatically or at the option of the Society or at the option of holders of such instruments. An offering of Additional CCDS and/or any such other instruments may have a dilutive effect on the holdings of CCDS holders either at the time of issue or upon their subsequent conversion into CCDS, including as regards the amount of any Distributions they may receive in respect of the CCDS and as regards the amounts (if any) which they may receive on a winding-up or dissolution of the Society, and could have an adverse effect on the market price of CCDS.

On a winding-up or dissolution of the Society, issues of Additional CCDS and/or such other instruments could have a dilutive effect on an investment in CCDS by reducing the amount of Surplus (if any) available for distribution to CCDS holders and/or by reducing the proportionate entitlement to Surplus of each CCDS.

There are no statutory, contractual or any other pre-emption rights in respect of the CCDS. Accordingly, holders of CCDS may be unable to avoid or mitigate the dilutive effects of issues of Additional CCDS or securities convertible into CCDS.

#### **Risks relating to an amalgamation by the Society with another building society or transfer of its business to another building society or a company**

The CCDS Conditions provide that, upon an amalgamation by the Society with another building society under section 93 of the Act or a transfer of all or substantially all of its engagements to another building society under section 94 of the Act, the CCDS shall become deferred shares in the amalgamated or transferee building society, as appropriate (the **Resulting Society**), having such terms and conditions as are necessary to ensure that both the CCDS and any other deferred shares which, prior to such amalgamation or transfer, constituted CET1 capital of the other society, shall constitute CET1 capital of the Resulting Society and, subject thereto, in all material respects identical to the terms of the CCDS, as determined by an independent financial adviser.

It may be necessary, in such circumstances, for the terms of the CCDS and/or the rules of the Resulting Society to be amended in certain respects and/or for certain adjustments to be made to the Cap on Distributions and/or the calculations and/or formulae relating to the rights of investors to share in any Surplus on a winding-up or dissolution of the Society. Whilst it is the intention of the Society that, if and to the extent that the Society has control over such matters, any such amendments and adjustments should be limited to the minimum necessary in order to ensure that the CCDS and any other deferred shares of the other society which, prior to such amalgamation or transfer, constituted CET1 capital of the other society, shall constitute CET1 capital of the Resulting Society, there can be no assurance that such amendments and adjustments will not have an adverse effect on the rights attaching to the CCDS and/or the market price of the CCDS.

In addition, upon a transfer by the Society of the whole of its business in accordance with section 97 of the Act to a company (a **Successor Entity**), the Successor Entity will assume a subordinated liability to each holder of CCDS which will be applied on or around the vesting date, on behalf of the CCDS holders, in the subscription of ordinary shares (which may or may not carry voting rights) in the Successor Entity or, if appropriate, any direct or indirect parent company of the Successor Entity. Whilst the number of shares to be delivered in such circumstance are required to have an aggregate market value as near as practicable to, but not less than, the market value of the CCDS immediately prior to the time of transfer of the business as determined by an independent financial adviser, there can be no assurance that the shares delivered in place of the CCDS will be as favourable in all respects to holders as the CCDS.

Furthermore, in the event of a demutualisation of the Society, there can be no assurance that the business model, risk approach or strategic ambition of the Successor Entity will be similar to that of the Society, and there can be no assurance that the holding of ordinary shares in a Successor Entity will

offer a similar risk profile or return on investment when compared with CCDS. For example, any dividend policy of the Successor Entity may be significantly different from the Board's Distribution Policy in respect of the CCDS. Furthermore, building societies are organised under the provisions of the Building Societies Act 1986, as amended (the **Act**) (see "*Part XX: Supervision and Regulation*"). The Act imposes a number of restrictions on the operation of a building society as compared to a bank, including (i) defining the purpose of a building society as "*that of making loans which are secured on residential property and funded substantially by its members*"; (ii) restricting the ability of building societies to engage in certain wholesale banking activities (for example, acting as a market maker in securities, commodities or currencies, trading in commodities or currencies, entering into certain transactions involving derivatives and limiting the risks for which derivatives hedging may be used); (iii) specifying certain limitations on the amount of non-mortgage lending that a building society is able to write (a minimum of 75 per cent. of loan assets, excluding liquid assets and fixed assets, must be secured on residential property); and (iv) limiting the volume of wholesale funding a building society may raise (at least 50 per cent. of funding (calculated in accordance with the Act) is required to be raised from retail depositors). A Successor Entity may not be constrained in these or similar respects under its governing legislation, and accordingly its business strategy could involve a greater degree of risk than that of the Society due to factors such as (but not limited to) increased risk appetite, a more aggressive approach to risk management, increased leverage, greater reliance on wholesale funding and/or unsecured lending and increased use of derivative investments or proprietary trading.

**Holders representing specified thresholds of outstanding CCDS may authorise the Society to vary the Conditions and, following a Regulatory Event, the Society is permitted to make certain amendments without any requirement for the consent of the holders. Any such amendments will be binding on all holders. Furthermore, the members of the Society are entitled to amend the Rules of the Society, and there can be no assurance that such amendments will not be materially prejudicial to the interests of the CCDS holders.**

The Conditions of the CCDS provide that such Conditions may be varied with the consent of the holders of the CCDS acting:

- (1) by written resolutions signed by or on behalf of CCDS holders holding in aggregate not less than three-quarters of the number of CCDS for the time being outstanding; or
- (2) at a quorate meeting of the CCDS holders, where not less than three-quarters of the number of the CCDS represented at such meeting are voted in favour of any proposed resolution. The quorum for any such meeting will be one or more persons representing in aggregate not less than one-third of the number of CCDS for the time being outstanding or, at an adjourned meeting and if such quorum is not otherwise present within half an hour from the time appointed for the adjourned meeting, the CCDS holders present in person or by proxy, irrespective of the number of CCDS represented.

Any resolutions approved by CCDS holders representing the requisite number of CCDS could have a significant adverse effect on the rights of CCDS holders and/or the value and/or market price of CCDS, and shall be binding on all CCDS holders, and the holders acting through the specified majorities have extensive powers to bind all CCDS holders.

In addition, following the occurrence of a Regulatory Event, the Society may vary the CCDS Conditions, without the need for any consent or approval of holders, so that they remain or become capable of qualifying in full as CET1 capital of the Society. Whilst such variations must not be materially less favourable to the CCDS holders than the terms immediately prior to such variations (as reasonably determined by the Society in good faith in consultation with an independent adviser of recognised standing), there can be no assurance that the CCDS, as varied, will be as favourable in all respects to the CCDS holders.

Furthermore, the CCDS Conditions do not limit the rights of members of the Society to amend the Rules. Whilst the Society undertakes in the CCDS Conditions not to initiate any amendment to the Rules that is both (a) inconsistent with the provisions of the CCDS Conditions and (b) materially prejudicial to the interests of the CCDS holders in that capacity, there can be no assurance that the members of the Society will not initiate and approve any such changes. The Conditions of the CCDS provide that, in the event that any changes which are materially prejudicial to the holders of the CCDS as a class are made to the Rules without the consent or approval of a requisite majority of CCDS holders, such changes shall not limit the rights of CCDS holders to bring an action for (or as if there had been a) breach of contract against the Society. However, there can be no assurance that such rights will afford adequate protection to CCDS holders in such circumstances and as a result holders of CCDS may experience material losses if the Rules are amended without their consent in a manner which is materially prejudicial to their interests.

**Transfers of CCDS are subject to a minimum transfer amount. CCDS holders who, as a result of trading CCDS, hold less than the minimum transfer amount in their accounts at any time will first need to purchase additional CCDS in order to enable them to transfer their existing holding of CCDS**

The CCDS will be transferable in whole numbers. The CCDS will be transferable only in amounts which are equal to or greater than a specified minimum transfer amount (the **Minimum Transfer Amount**) prevailing from time to time. The Minimum Transfer Amount is fixed at 500 CCDS and will not be reduced except in agreement with the Relevant Regulators. Purported trades of CCDS in a number less than the Minimum Transfer Amount prevailing at the relevant time will not be valid. If an investor, as a result of trading CCDS, holds less than the Minimum Transfer Amount in its clearing system or custodian account, it will first need to purchase additional CCDS in order to enable it to transfer its existing holding of CCDS.

It will not be possible for investors to transfer CCDS in amounts less than the Minimum Transfer Amount prevailing as at the time of transfer. The Clearing Systems will not accept instructions to settle transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount, and (in the limited circumstances in which definitive CCDS are issued) the Registrar will not register in the CCDS Register any transfer of CCDS in definitive form in amounts less than the prevailing Minimum Transfer Amount. Accordingly, purported transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount will be incapable of settlement.

Investors in CCDS are responsible for ensuring that any trades they enter into in respect of the CCDS are capable of settlement; failure to do so may result in an investor breaching its contract of sale and purchase.

**Investors in the CCDS will hold beneficial interests in the CCDS through an account with a Clearing System, will not be members of the Society by virtue of their investment in CCDS and must rely on the relevant Clearing System's procedures**

The CCDS will be represented by a global certificate registered in the name of Citivic Nominees Limited as nominee (the **Nominee**) for the Clearing Systems. Investors in the CCDS will hold beneficial interests in the CCDS through an account with a Clearing System. However, the Nominee shall be the sole owner of legal title to the CCDS represented by the global certificate, and shall be the registered holder for those CCDS for the purposes of the Rules and the CCDS Conditions.

Accordingly, an investor holding beneficial interests in the CCDS through an account with a Clearing System will not become a member of the Society by virtue of its investment in the CCDS and will only indirectly benefit from the CCDS Conditions, the Rules, the Memorandum and the Act with respect to the CCDS through the Nominee. Such investor shall be entitled to rights in respect of its beneficial interest in the CCDS as prescribed by the rules of the relevant Clearing System and must rely on the

procedures of the Clearing Systems to enforce its rights. The Society has no responsibility or liability for the records relating to beneficial interests in any CCDS.

The terms of the global certificate evidencing the CCDS provide that definitive CCDS will only be issued outside the Clearing Systems and registered directly in the name of each investor in the event that all Clearing Systems have closed for business, which the Directors consider unlikely to occur.

The holding structure for CCDS has a number of consequences for investors, including with respect to member voting rights and rights to conversion benefits in the event of a demutualisation of the Society, as further described in the following two risk factors.

**Investors will have no voting rights at general meetings of the members of the Society for so long as the CCDS are held through an account with a Clearing System**

In contrast to general meetings of shareholders of a limited company where shareholders may exercise voting rights which are proportionate to the number of shares they hold, at a general meeting of the members of the Society, each member is, in line with the principles of mutuality, entitled to only one vote (or, in applicable circumstances, one vote in its capacity as an investing member and one vote in its capacity as a borrowing member) regardless of the size or number of its investments or interests in the Society. Only a member of the Society is entitled to vote at general meetings.

For so long as any CCDS are held by the Nominee for and on behalf of the Clearing Systems, the Nominee shall be the only member of the Society in respect of those CCDS, and in its capacity as a member shall have only one vote at general meetings of the members of the Society (regardless of the number of CCDS it holds and regardless also of the size and number of any other relevant investments or interests (if any) it may have in the Society). Given the difficulty of casting its one vote in a manner which reflects the views of all the investors holding CCDS in an account with a Clearing System and the insignificance of that vote in the context of all the votes which may be cast by members of the Society, the Nominee has informed the Society that it does not intend to exercise its vote insofar as it relates to its holding of CCDS.

Further, even if definitive CCDS were to be issued and delivered outside the Clearing Systems in the limited circumstances described above (in which case, the CCDS would be registered in the name of each holder directly and would confer membership rights directly upon each registered holder) each holder of definitive CCDS would be entitled to exercise only one vote (or, if applicable depending upon the circumstances of that particular member, one vote in its capacity as an investing member and one vote in its capacity as a borrowing member) at a general meeting of the members of the Society (subject to qualifying as a voting member under the Society's rules), regardless of the number of CCDS held by such holder and regardless also of the size and number of any other relevant investments or interests such holder may have in the Society. In circumstances where definitive CCDS are issued and a holder of CCDS derives its membership of the Society solely from its registered holding of CCDS, such holder will only be able to exercise its member vote at a general meeting of the Society if it held CCDS (a) at the end of the Society's financial year before the voting date, or (b) on the voting qualification date and (c) on the voting date and (d) such holder must not have ceased to hold CCDS between the dates specified in (a) or (b) (as applicable) and the voting date.

Accordingly, investors in CCDS will not, by virtue of their investment, have any voting rights at general meetings of the members of the Society unless definitive CCDS are issued and delivered (which the Directors consider is unlikely) in which case the limited voting rights acquired by each investor would be entirely insignificant in the context of the number of votes which could be cast by members of the Society as a whole.

For the avoidance of doubt, the foregoing paragraphs relate to voting rights as member at general meetings of the Society. The CCDS Conditions contain provisions which enable separate meetings to be convened of the CCDS holders as a class only, for the purposes of considering matters affecting the

rights of the CCDS holders. At such class meetings only, investors in the CCDS will be entitled to exercise one vote for each CCDS held by such investor at the relevant time. Investors should note that such provisions provide that CCDS holders holding defined majorities of the number of CCDS outstanding are able to agree, by resolution in writing or passed at a duly convened meeting of the CCDS holders, to amendments to the CCDS Conditions which shall bind all CCDS holders, including those who do not vote in favour of the relevant resolution.

**For so long as the CCDS are held in an account with a Clearing System, the Holders thereof will not be entitled to Conversion Benefits arising on a demutualisation or other transfer of the Society's business to a company**

As investors will hold their CCDS through accounts with the Clearing Systems and thus will not be members of the Society by virtue of their investment in CCDS, they will also not be entitled, by virtue of their investment in CCDS, to any Conversion Benefits (being benefits under the terms of any future transfer of the Society's business to a company, other than rights to receive ordinary shares issued by the successor entity or its parent, as specifically provided for under CCDS Condition 10) arising on a demutualisation or other transfer of the Society's business to a company. Any Conversion Benefits arising on any such transaction will belong instead to the Nominee, as the registered holder of the CCDS. The Nominee will, on or prior to the date of issue of the CCDS, agree to assign to a selected charity nominated by the Society pursuant to any scheme for charitable assignment established by the Society any Conversion Benefits to which it would otherwise become entitled at any time.

Even if definitive CCDS were to be issued in the limited circumstances described under "*Investors in the CCDS will hold beneficial interests in the CCDS through an account with a Clearing System, will not be members of the Society by virtue of their investment in CCDS and must rely on the relevant Clearing System's procedures*" above, each holder of definitive CCDS would have no right to retain any Conversion Benefits and would be required pursuant to the CCDS Conditions to assign any Conversion Benefits to (or waive its right to receive any Conversion Benefits in favour of) the Society.

**Transfers of the CCDS with the Clearing Systems may become liable to UK stamp duty reserve tax**

The CCDS will constitute "chargeable securities" for UK stamp duty reserve tax (SDRT) purposes. However, on the basis of current United Kingdom tax law, transfers of CCDS within the Clearing Systems should not be subject to SDRT provided that no election is or has been made under section 97A of the Finance Act 1986 (a **97A election**) by the relevant Clearing System that applies to the CCDS. The Society has received confirmation from each Clearing System that the CCDS would be admitted to its systems without a 97A election applying to the CCDS. However, if a 97A election were to apply to the CCDS in the future, transfers of the CCDS within the Clearing Systems could, unless an exemption applies, be subject to SDRT (currently at the rate of 0.5 per cent. of the consideration given under the agreement to transfer the CCDS).

#### **4. RISKS RELATED TO THE TIER 2 NOTES**

*Capitalised terms used and not otherwise defined in this section 4 (Risks related to the Tier 2 Notes) have the meaning given to them in "Part X: Terms and Conditions of the Tier 2 Notes" of these Listing Particulars.*

**The Tier 2 Notes constitute direct, unsecured and subordinated obligations of the Society and will rank junior to most liabilities of the Society**

Whilst claims in respect of the Tier 2 Notes will, in the event of the winding up or dissolution of the Society (other than an Excluded Dissolution), rank in priority to claims in respect of the CCDS, the claims in respect of principal, interest and any other amount (including, without limitation, any damages awarded for breach of the Society's obligations) in respect of the Tier 2 Notes will be

subordinated in right of payment to (i) all senior claims in respect of the Society (including the claims of all unsubordinated creditors and of all members of the Society in respect of principal and interest due on their shares other than deferred shares), (ii) all senior non-preferred claims in respect of the Society, and (iii) those subordinated claims (if any) in respect of the Society which rank, or are expressed to rank, in priority to claims in respect of the Tier 2 Notes.

Accordingly, if the Society is wound up, the Society will be required to meet its obligations to all of its creditors (including all of its UK retail member deposits) that are afforded higher-priority status in full before it can make any payments in respect of the Tier 2 Notes. If the Society does not have enough assets to meet all of the more senior-ranking claims in a winding up, the holders of Tier 2 Notes will lose their entire investment in those Tier 2 Notes. If the Society has sufficient assets to meet all of the more senior-ranking claims but not all claims of the Tier 2 Note holders and any other claims ranking equally with those claims, investors in the Tier 2 Notes will lose some (which may be substantially all) of their investment in their Tier 2 Notes.

Furthermore, the ranking of the Tier 2 Notes in a winding up can also be expected to have a direct impact on the relative losses imposed on holders of Tier 2 Notes in a resolution of the Society or a capital write-down under the Banking Act, as such resolution and capital write-down powers ought to be used in a manner that mirrors the hierarchy of claims in an ordinary insolvency - see *“The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK deposit-taking institutions which are considered to be at risk of failing. The exercise of any of these actions in relation to the Society and/or the CCDS and/or Tier 2 Notes could materially adversely affect the value of any Securities and the rights of the holders thereof”*.

#### **Limitation on gross-up obligation**

The Society’s obligation to pay additional amounts in respect of any withholding or deduction in respect of UK taxes applies only to payments of interest due and payable under the Tier 2 Notes and not to payments of principal. As such, the Society would not be required to pay any additional amounts to the extent any withholding or deduction for or on account of UK tax applied to payments of principal. Accordingly, if any such withholding or deduction were to apply to any payments of principal, holders of the Tier 2 Notes would, upon repayment or redemption, be entitled to receive only the net amount of such redemption or repayment proceeds after deduction of the amount required to be withheld. Therefore, holders may receive less than the full amount due under the Tier 2 Notes, payment of the net amount would discharge the Society’s obligations in respect of the relevant payment in full, and the market value of the Tier 2 Notes may be adversely affected.

#### **The remedies available to holders under the Tier 2 Notes are very limited**

The remedies under the Tier 2 Notes are very limited. If the Society fails to make any payment on the Tier 2 Notes when due or within a short grace period thereafter, holders will be entitled to institute proceedings for the winding up of the Society and to claim in that winding up, but will have no other means to enforce any amounts owing under the Tier 2 Notes, and no amounts in respect of the Tier 2 Notes may be accelerated except in a winding up of the Society. Since, as described under *“The Tier 2 Notes constitute direct, unsecured and subordinated obligations of the Society and will rank junior to most liabilities of the Society”* above, claims in respect of the Tier 2 Notes will, in a winding up of the Society, be subordinated to most liabilities of the Society, there can be no assurance that any enforcement action taken by Tier 2 Note holders in the event of non-payment or a winding up of the Society will result in them recovering any amounts from the Society, in particular if the Society is insolvent.

#### **There is no limit on the amount or type of further indebtedness that the Society may incur**

There is no restriction on the amount of debt instruments or other liabilities that the Society may issue, incur or guarantee and which rank senior to, or *pari passu* with, the Tier 2 Notes. The issue or



guaranteeing of any such debt instruments or the incurrence of any such other liabilities may reduce the amount (if any) recoverable by holders of Tier 2 Notes in the event of a winding-up, dissolution or resolution of the Society and may limit the Society's ability to meet its obligations under the Tier 2 Notes. The Society may also issue subordinated liabilities which rank senior to the Tier 2 Notes.

**Holders may not require the redemption of the Tier 2 Notes prior to their maturity**

The Tier 2 Notes mature on 12 April 2038. The Society is under no obligation to redeem or purchase the Tier 2 Notes at any time prior thereto and the holders have no right to require the Society to redeem or purchase any Tier 2 Notes at any time prior to their maturity. Any redemption of the Tier 2 Notes and any purchase of any Tier 2 Notes by the Society will be subject always to the prior approval of the Supervisory Authority and to compliance with prevailing Regulatory Capital Requirements.

Accordingly, holders of Tier 2 Notes wishing to realise their investment prior to the maturity date would need to sell their Tier 2 Notes to a market purchaser. Whilst the Society intends to apply to the Luxembourg Stock Exchange for the Tier 2 Notes to be admitted to the Official List of the Luxembourg Stock Exchange and to listing on the Euro MTF, there can be no assurance that a secondary market in the Tier 2 Notes will be established and, if any such market is established, it may be illiquid and prices may be volatile. The market price of the Tier 2 Notes will also be affected by many factors, including the actual or perceived ability of the Society to meet its obligations in respect of the Tier 2 Notes. Accordingly, even if a holder is able to sell Tier 2 Notes in a secondary market, there can be no assurance that the price of such sale would enable the investor to recover its initial investment, and the investor may suffer significant losses on its investment if the market price is lower than the price at which such investor acquires Tier 2 Notes. Investors in the Tier 2 Notes should be prepared to hold their Tier 2 Notes for a significant period of time.

**The Tier 2 Notes are subject to early redemption at the option of the Society from 2033, and may also be redeemed by the Society at any time (including before such date) upon the occurrence of certain tax and regulatory events**

Subject to the prior approval of the Supervisory Authority and to compliance with prevailing Regulatory Capital Requirements, the Society may, at its option, redeem all (but not some only) of the Tier 2 Notes at their principal amount plus accrued and unpaid interest on 12 April 2033 or any Interest Payment Date thereafter. In addition, subject to the prior approval of the Supervisory Authority and to compliance with prevailing Regulatory Capital Requirements, the Society may, at its option, redeem all (but not some only) of the Tier 2 Notes at their principal amount plus accrued and unpaid interest at any time (whether before or after 12 April 2033) upon the occurrence of a Tax Event or a Capital Disqualification Event.

Such optional redemption features are likely to limit the market value of the Tier 2 Notes. During any period when the Society may (or the market perceives that the Society is or may become entitled to) elect to redeem the Tier 2 Notes, the market value of the Tier 2 Notes generally will not rise substantially above the price at which they can be redeemed. This also may be true prior to any redemption period. Further, during periods when there is an increased likelihood, or perceived increased likelihood, that the Tier 2 Notes will be redeemed early, the market value of the Tier 2 Notes may be adversely affected.

The Society may be more likely to exercise its option to redeem the Tier 2 Notes at times when it could refinance at a lower cost than the prevailing interest rate payable in respect of the Tier 2 Notes. Accordingly, holders may only be able to reinvest the redemption proceeds in securities with a lower yield. Potential investors should consider reinvestment risk in light of other investments available at that time.

## **The Society may be substituted as principal debtor in respect of the Tier 2 Notes**

At any time the Society may, subject to certain conditions being complied with, be substituted for another entity as the principal debtor under the Tier 2 Notes, without the consent of the holders of the Tier 2 Notes. The Act imposes a number of restrictions on the operation of a building society as compared to a bank, including (i) defining the purpose of a building society as “*that of making loans which are secured on residential property and funded substantially by its members*”; (ii) restricting the ability of building societies to engage in certain wholesale banking activities (for example, acting as a market maker in securities, commodities or currencies, trading in commodities or currencies, entering into certain transactions involving derivatives and limiting the risks for which derivatives hedging may be used); (iii) specifying certain limitations on the amount of non-mortgage lending that a building society is able to write (a minimum of 75 per cent. of loan assets, excluding liquid assets and fixed assets, must be secured on residential property); and (iv) limiting the volume of wholesale funding a building society may raise (at least 50 per cent. of funding (calculated in accordance with the Act) is required to be raised from retail depositors). A successor entity may not be constrained in these or similar respects under its governing legislation, and accordingly its business strategy could involve a greater degree of risk than that of the Society due to factors such as (but not limited to) increased risk appetite, a more aggressive approach to risk management, increased leverage, greater reliance on wholesale funding and/or unsecured lending and increased use of derivative investments or proprietary trading.

## **As the Tier 2 Notes bear a fixed rate of interest, their value in the market may be adversely affected by movements in market interest rates**

Investment in securities, such as the Tier 2 Notes, which bear a fixed rate of interest involves the risk that if market interest rates increase, including if at any time they are or increase above the rate paid on such securities, this will adversely affect their value.

## **Meetings of holders and modification**

The Conditions of the Tier 2 Notes will contain provisions for calling meetings of holders to consider matters affecting their interests generally. These provisions permit defined majorities to bind all holders including holders who did not attend and vote at the relevant meeting and holders who voted in a manner contrary to the majority. Any matters so approved by the requisite majority of holders could have a significant adverse impact on the rights attaching to the Tier 2 Notes and/or their value and/or market price.

In addition, the Tier 2 Agent may agree with the Society, without the consent of the holders, to make any modification to any of the Conditions of the Tier 2 Notes or any of the provisions of the Tier 2 Agency Agreement that, in the Society’s opinion: (i) is not materially prejudicial to the interests of the holders; or (ii) its opinion, is of a formal, minor or technical nature or to correct a manifest error or to comply with mandatory provisions of the law. Any such modification shall be binding on the holders.

The Tier 2 Notes will be subordinated liabilities and will not confer any membership rights on holders. Holders of the Tier 2 Notes will not (in that capacity) be entitled to attend or vote at general meetings of the members of the Society.

## **Integral multiples of less than £1,000**

The denominations of the Tier 2 Notes will be £1,000 and integral multiples of £100 in excess thereof. Accordingly, it is possible that the Tier 2 Notes may be traded in the clearing systems in amounts in excess of £1,000 that are not integral multiples of £1,000. Should certificates representing the Tier 2 Notes in definitive form be required to be issued, they will be issued in principal amounts of £1,000 and higher integral multiples of £100 but will in no circumstances be issued to holders who hold Tier 2 Notes in the Clearing Systems in amounts that are less than £1,000. Accordingly, any holder who holds

an amount which is less than £1,000 in principal amount of the Tier 2 Notes in his account with the relevant Clearing System at the relevant time may not receive a certificate (should certificates be printed) in respect of such holding. Such a holder would need to purchase a principal amount of Tier 2 Notes such that its holding amounts to £1,000 in order to receive a certificate.

If Certificates are issued, holders should be aware that Tier 2 Notes which have a denomination that is not an integral multiple of £1,000 may be illiquid and difficult to trade.

## 5. RISKS RELATED TO ALL SECURITIES

**The Banking Act confers substantial powers on a number of UK authorities designed to enable them to take a range of actions in relation to UK deposit-taking institutions which are considered to be at risk of failing. The exercise of any of these actions in relation to the Society and/or the CCDS and/or Tier 2 Notes could materially adversely affect the value of any Securities and the rights of the holders thereof**

Under the Banking Act, substantial powers are granted to HM Treasury, the PRA, the FCA and the Bank of England (together, the **Authorities**) as part of a special resolution regime (the **SRR**). These powers enable the Authorities to deal with, amongst other entities, a UK bank or building society (each a **relevant entity**) in circumstances in which the Authorities consider that the resolution conditions are satisfied, through a series of stabilisation options.

The stabilisation options which may be commenced by the Authorities are: (i) private sector transfer of all or part of the business of the relevant entity; (ii) transfer of all or part of the business of the relevant entity to a “bridge bank” established by the BoE; (iii) transfer to an asset management vehicle; (iv) temporary public ownership (nationalisation) of the relevant entity including powers to convert a building society into a company in connection with a bail-in; and (v) a bail-in tool which permits the BoE to (a) cancel, modify or convert the form of a liability owed by a relevant entity or provide that a contract under which, amongst others, a relevant entity has a liability is to have effect as if a specified right had been exercised under it, or (b) transfer securities issued by a relevant entity to a bail-in administrator.

In each case, the Authorities have wide powers under the Banking Act including powers to modify contractual arrangements in certain circumstances and powers for HM Treasury to disapply or modify laws (with possible retrospective effect) to enable the powers under the Banking Act to be used effectively.

The BRRD also provides for a Member State as a last resort, after having assessed and used the above resolution tools to the maximum extent practicable whilst maintaining financial stability, and where certain other mandatory conditions of the BRRD have been satisfied, may provide extraordinary public financial support through additional financial stabilisation tools. These consist of the public equity support and temporary public ownership tools. Any such extraordinary financial support must be provided in accordance with the EU state aid framework.

In addition, the Banking Act contains a separate power, often referred to as the “capital write-down tool”, enabling the BoE to cancel or transfer Common Equity Tier 1 instruments (such as the CCDS) away from the original owners, or write down (including to nil) an institution’s Additional Tier 1 and Tier 2 capital instruments (such as the Tier 2 Notes), or to convert them into Common Equity Tier 1 instruments (which, in the case of the Society, could be Additional CCDS), if the Authorities consider that the institution or the group is at the “point of non-viability” and certain other conditions are met. The capital write-down tool must be applied before any of the stabilisation options provided for in the SRR may be used in practice and may be used whether or not the institution subsequently enters into resolution. In addition, the capital write-down tool must be used either before or concurrently with the resolution tools.

Accordingly, the use of any stabilisation powers in respect of the Society may have an adverse effect on its ability to declare Distributions in respect of the CCDS and/or perform its obligations in respect of the Tier 2 Notes, and the use of any stabilisation powers and/or the capital write-down tool in respect of CCDS and/or the Tier 2 Notes themselves may impact their market price and/or may adversely affect the rights of the holders of such Securities. These risks are discussed further in the following paragraphs.

*The SRR and/or capital write-down tool may be triggered prior to insolvency of the Society*

The purpose of the stabilisation options and the capital write-down powers is to address the situation where all or part of a business of a relevant entity has encountered, or is likely to encounter, financial difficulties, giving rise to wider public interest concerns. Accordingly, the stabilisation options may be exercised if (i) the BoE is satisfied that a relevant entity (such as the Society) is failing or is likely to fail, (ii) having regard to timing and other relevant circumstances, the relevant Authority determines that it is not reasonably likely that (ignoring the stabilisation powers) action will be taken that will enable the relevant entity to satisfy those conditions, (iii) the BoE considers the exercise of the stabilisation options to be necessary, having regard to certain public interest considerations (such as the stability of the UK financial system, public confidence in the UK banking system and the protection of depositors) and (iv) the BoE considers that the specific resolution objectives would not be met to the same extent by the winding up of the relevant entity.

It is therefore possible that one or more of the stabilisation options could be applied prior to the point at which any insolvency proceedings with respect to the relevant entity could be initiated.

The EBA has published guidelines on the circumstances in which an institution shall be deemed as “failing or likely to fail” by supervisors and resolution authorities. The guidelines set out the objective criteria which should apply when supervisors and Authorities make such a determination.

Although the Banking Act provides for conditions to the exercise of any resolution powers and the EBA guidelines set out the objective elements for determining whether an institution is failing or likely to fail, it is uncertain how the Authorities would assess such conditions in any particular situation. The relevant Authorities are also not required to provide any advance notice to holders of the CCDS or the Tier 2 Notes of their decision to exercise any resolution power. Therefore, the holders may not be able to anticipate a potential exercise of any such powers nor the potential effect of any exercise of such powers on the Society or the Securities.

*Various actions may be taken in relation to the CCDS and/or the Tier 2 Notes without the consent of the holders*

If the Society were made subject to the SRR, HM Treasury or the Bank of England may exercise extensive share transfer powers (applying to a wide range of securities) and property transfer powers (including powers for partial transfers of property, rights and liabilities) in respect of the Society and/or its securities (subject to certain protections).

Exercise of these powers could involve taking various actions in relation to any securities issued by the Society, including the CCDS and Tier 2 Notes, without the consent of the holders, including (among other things):

- transferring the CCDS and the Tier 2 Notes out of the hands of the holders;
- delisting the CCDS and the Tier 2 Notes;
- cancelling the CCDS and/or writing down (which may be to nil) the Tier 2 Notes or converting the Tier 2 Notes into CCDS (or another form or class of securities); and/or

- modifying or disapplying certain terms of the Securities, which could relate to fundamental terms such as interest rates or payment dates, the ability to pay distributions, maturity dates, call rights, enforcement rights or other terms.

The relevant Authorities may exercise the bail-in tool under the Banking Act to recapitalise a relevant entity in resolution by allocating losses to (amongst others) its capital providers and unsecured creditors (which would include holders of the CCDS and the Tier 2 Notes) in a manner that (i) ought to respect the hierarchy of claims in an ordinary insolvency and (ii) is consistent with members and creditors not receiving a less favourable treatment than they would have received in ordinary insolvency proceedings of the relevant entity (known as the “no creditor worse off” safeguard) (although this safeguard will not necessarily be available in respect of capital instruments such as CCDS and Tier 2 Notes). Accordingly, the ranking of CCDS and the Tier 2 Notes in insolvency can be expected to have a direct impact on the relative losses imposed on holders of those Securities in a resolution. For further information with respect to the ranking of the CCDS, see “*The CCDS are deeply subordinated instruments and holders of the CCDS will be entitled to only a limited share in any surplus assets of the Society on a winding-up of the Society*” above, and for further information with respect to the ranking of the Tier 2 Notes, see “*The Tier 2 Notes constitute direct, unsecured and subordinated obligations of the Society and will rank junior to most liabilities of the Society*” above.

The bail-in tool includes the power to cancel a liability or modify the terms of contracts for the purposes of reducing or deferring the liabilities of the relevant entity under resolution and the power to convert a liability from one form or class to another. There is also the power to convert a building society into a company in connection with a bail-in. The exercise of such powers may result in the cancellation of all, or a portion, of the principal amount of, interest on, or any other amounts payable on or in respect of, the CCDS and/or the Tier 2 Notes and/or result in the CCDS and/or Tier 2 Notes being cancelled or otherwise transferred, exchanged or varied in a manner which imposes significant losses on holders.

The taking of any such actions could materially adversely affect the rights of holders of the CCDS and the Tier 2 Notes, the price or value of their investment in such Securities, the liquidity and/or volatility of any market in such Securities and/or the ability of the Society to make payments in respect of, or otherwise satisfy its obligations under, such Securities. In such circumstances, there can be no assurance that holders will have any claim for compensation under one of the compensation schemes existing under, or contemplated by, the Banking Act.

In addition, if the market perceives or anticipates that any action may be taken under the Banking Act in respect of the Society or any of its securities (including the CCDS and/or the Tier 2 Notes), this may have a significant adverse effect on the market price (if any) of such Securities and/or the liquidity and/or volatility of any market in them, whether or not such powers are ultimately exercised. In such case, investors may experience difficulty in selling their Securities, or may only be able to sell their Securities at a loss.

#### *Mandatory write-down and conversion of capital instruments may affect the CCDS and the Tier 2 Notes*

As noted above, in addition to the stabilisation options which may be used in a resolution of an institution, the Banking Act contains a capital write-down tool which enables (and, if the institution enters into resolution, requires) the relevant Authorities permanently to cancel, write-down, or convert into Common Equity Tier 1 instruments (such as CCDS), any Tier 1 capital instruments (including the CCDS) and Tier 2 capital instruments (including the Tier 2 Notes) at the point of non-viability of the relevant entity and before or together with the exercise of any stabilisation power.

For the purposes of the application of such mandatory write-down and conversion power, the point of non-viability is the point at which the relevant Authority determines that the relevant entity meets the conditions for resolution (but no resolution action has yet been taken) or that the relevant entity will no

longer be viable unless the relevant capital instruments are written-down or converted or the relevant entity requires extraordinary public support without which, the relevant UK resolution authority determines that, the relevant entity would no longer be viable.

The CCDS and the Tier 2 Notes could be the subject of exercise of these powers, resulting in the holders losing some or all of their investment. The Society understands that the “no creditor worse off” safeguard would not apply in relation to an application of such powers in circumstances where resolution powers are not also exercised.

The exercise of such mandatory write-down and conversion power under the Banking Act could, therefore, materially adversely affect the rights of holders of CCDS and/or Tier 2 Notes, and such exercise (or the perception that such exercise may occur) could materially adversely affect the price or value of their investment in such Securities and/or the ability of the Society to make payments or otherwise satisfy its obligations under the Securities, and/or may adversely affect liquidity and/or volatility in the market (if any) for such Securities.

*The circumstances under which the relevant UK resolution authority would exercise its resolution and capital write-down powers are uncertain*

There is considerable uncertainty regarding the specific factors beyond the goals of addressing banking crises pre-emptively and minimising taxpayers' exposure to losses (for example, by writing down relevant capital instruments before the injection of public funds into a financial institution) which the relevant UK resolution authority would consider in deciding whether to exercise the capital write-down, bail-in or other resolution powers with respect to the Society and/or its securities, including the CCDS and the Tier 2 Notes. While the Banking Act provides some guidance as to how and when the bail-in option may be utilised by the relevant UK resolution authority, the Banking Act and the BRRD (which has been transposed into UK law by way of amendments to the Banking Act) allow for discretion and there is no certainty as to how the relevant UK resolution authority will exercise such discretion. As there may be many factors, including factors outside of the Society's control or not directly related to it, which could result in such a determination, holders of the Securities may not be able to refer to publicly available criteria in order to anticipate a potential exercise of any such UK bail-in power.

Accordingly, the threat of capital write-down, bail-in or other resolution powers may affect trading behaviour, including prices and volatility, and, as a result, the Securities are not necessarily expected to follow the trading behaviour associated with other types of securities.

**Any change in English law or administrative practice or in United Kingdom taxation laws or practice that affects the Securities could be prejudicial to the interests of holders of the Securities**

The Conditions of the Securities are based on English law in effect as at the date of these Listing Particulars. No assurance can be given as to the impact on the holders of the Securities of any possible judicial decision or change to English law or administrative practice or in United Kingdom taxation laws or practice after the date of these Listing Particulars.

**The trading price of the Securities may fluctuate which could lead to investors losing some or all of their investment**

The trading price of the Securities in the secondary markets (if any such price continues to be quoted) may be subject to wide fluctuations in response to many factors, including those referred to in this risk factor, as well as stock market fluctuations and general economic conditions that may adversely affect the market price of the Securities. Publicly traded securities from time to time experience significant price and volume fluctuations that may be unrelated to the operating performance of the companies that have issued them, and such volatility may be increased in an illiquid market. Accordingly, the market price of the Securities may prove to be highly volatile. The market price of the Securities may fluctuate

significantly in response to a number of factors, some of which are beyond the Society's control, including (but not limited to) the following:

- material decreases in the Society's capital ratios which could arise as a result of a number of factors including changes in regulation or losses incurred by the Society;
- changes (or expected changes) to the Board's Distribution Policy in respect of the CCDS, or any decision by the Board to depart from its Distribution Policy;
- variations in operating results in the Society's reporting periods;
- any shortfall in revenue or net profit or any increase in losses from levels expected by market commentators;
- increases in capital expenditure compared with expectations;
- any perception that the Society's strategy is or may be less effective than previously assumed or that the Society is not effectively implementing any significant projects;
- changes in financial estimates by securities analysts;
- changes in market valuations of similar entities;
- announcements by the Society of significant acquisitions, strategic alliances, joint ventures, new initiatives, new services or new service ranges;
- regulatory matters;
- additions or departures of key personnel;
- any election by the Society not to declare a Distribution in respect of any given financial year, or the declaration of a Distribution which is lower than that expected by the market; and
- future issues or sales of CCDS, Tier 2 Notes or other securities.

Any or all of these events could result in material fluctuations in the price of Securities, significantly increased price volatility and/or changes in the trading behaviour and performance of Securities, which could lead to investors losing some or all of their investment.

In addition, investors in the Securities should not necessarily expect the price of the Securities to vary in response to factors that affect the UK financial services industry generally, such as, for example, changes in Bank of England base rates.

The initial issue price of the Securities might not be indicative of prices that will prevail in the trading market and investors may not be able to resell their Securities at or above the price at which they purchased Securities.

### **Legality of purchase**

The Society neither has nor assumes responsibility for the lawfulness of the acquisition of the Securities by a prospective investor in the Securities, whether under the laws of the jurisdiction of its incorporation or the jurisdiction in which it operates (if different), or for compliance by that prospective investor with any law, regulation or regulatory policy applicable to it.

### **Legal investment considerations may restrict certain investments**

The investment activities of certain investors are subject to legal investment laws and regulations, or review or regulation by certain authorities. Each potential investor should consult its legal advisers to determine whether and to what extent (i) Securities are legal investments for it, (ii) Securities can be used as collateral for various types of borrowing and (iii) other restrictions apply to its purchase or pledge of any Securities. Financial institutions should consult their legal advisers or the appropriate regulators to determine the appropriate treatment of Securities under any applicable risk-based capital or similar rules.

### **The Securities are not protected liabilities of the Society and holders of the Securities will not therefore benefit from the Financial Services Compensation Scheme**

The FSCS is described in paragraph 2.8 “*Financial Services Compensation Scheme*” of “*Part XX: Supervision and Regulation*” as the statutory fund of last resort for customers of authorised financial services firms, such as the Society, paying compensation to customers if the Society is unable, or likely to be unable, to pay certain claims (including in respect of deposits and insurance policies) made against it (together, **Protected Liabilities**).

However, **neither the CCDS nor the Tier 2 Notes are Protected Liabilities of the Society** and, accordingly, investors in the Securities will not have recourse to the FSCS for any amount in respect of their investment in CCDS or Tier 2 Notes in the event that the Society becomes insolvent.

Moreover, the Securities are not guaranteed or insured by any government, government agency or compensation scheme of the UK or any other jurisdiction.

### **An investment in Securities by an investor whose principal currency is not sterling may be affected by exchange rate fluctuations**

The Securities are denominated, and any Distributions in respect of the CCDS and interest in respect of the Tier 2 Notes will be paid, in sterling. An investment in Securities by an investor whose principal currency is not sterling exposes the investor to foreign currency exchange rate risk. Any depreciation of sterling in relation to such foreign currency will reduce the value of the investment in the Securities or any Distribution (in relation to the CCDS) or interest payment (in relation to the Tier 2 Notes) in relation to such foreign currency.

### **Because the Securities are held by or on behalf of the Clearing Systems investors will have to rely on the Clearing System procedures for transfer, payment and communication with the Society**

The CCDS and the Tier 2 Notes will, upon issue, be represented by the Global CCDS Certificate and the Global Tier 2 Certificate, respectively, that will be deposited with, and registered in the name of the Nominee, and the Clearing Systems will maintain records of the beneficial interests in the Global Certificates. While the Securities are in global form, investors will be able to trade their beneficial interests only through the Clearing Systems.

While the Securities are in global form, the payment obligations of the Society under the Securities will be discharged upon such payments being made by or on behalf of the Society to or to the order of the nominee for the common depositary. A holder of a beneficial interest in a Security must rely on the Clearing Systems’ procedures to receive payments under the Securities. The Society does not have any responsibility or liability for the records relating to, or payments made in respect of, beneficial interests in the Global Certificates.



## PART II – OVERVIEW OF THE SECURITIES

The following overview does not purport to be complete and is taken from, and is qualified in its entirety by, “Part IX: *Conditions of Issue of the Core Capital Deferred Shares*” and “Part X: *Terms and Conditions of the Tier 2 Notes*” of these Listing Particulars.

Words and expressions defined in “Part IX: *Conditions of Issue of the Core Capital Deferred Shares*” and “Part X: *Terms and Conditions of the Tier 2 Notes*” of these Listing Particulars shall have the same meanings in this Overview. References to the **Conditions** shall mean the Conditions of Issue of the Core Capital Deferred Shares or the Terms and Conditions of the Tier 2 Notes, as applicable, and references to a numbered **Condition** shall be construed accordingly.

### Overview of the Core Capital Deferred Shares

<b>Issuer</b>	The Society.
<b>Securities</b>	Core Capital Deferred Shares.
<b>Currency</b>	British pounds sterling (£).
<b>Nominal amount</b>	£1 per CCDS.
<b>Issue Price</b>	£100 per CCDS (representing £1 of Nominal Amount and £99 of premium per CCDS).
<b>Minimum Investment Amount</b>	The minimum permitted investment in CCDS pursuant to the LME is £50,000 (representing 500 CCDS at the Issue Price).
<b>Minimum Transfer Amount</b>	Transfers of CCDS (or beneficial entitlements therein) will not be valid unless the number of CCDS transferred is a whole number that is equal to or greater than the minimum transfer amount prevailing at the time of transfer. The minimum transfer amount is fixed at 500 CCDS (or such other amount as may be required by the PRA or the FCA) and will not be reduced except in agreement with the PRA and the FCA.
<b>Status and Subordination</b>	<p>The CCDS will constitute direct, unsecured and subordinated investments in the Society and, on a winding-up or dissolution of the Society, will rank (a) <i>pari passu</i> among themselves and with any other investments ranking or expressed to rank <i>pari passu</i> with the CCDS (provided that participation of CCDS holders in the Surplus will be in the manner and proportion described in the conditions of the CCDS), and (b) junior to (i) all Liabilities of the Society and (ii) any claims in respect of declared, unconditional and unpaid periodic Distributions and claims ranking or expressed to rank <i>pari passu</i> therewith.</p> <p>The CCDS will rank junior to the PIBS and the Tier 2 Notes of the Society.</p> <p>The CCDS will be deferred shares for the purposes of section 119 of the Building Societies Act 1986, as amended.</p>
<b>Waiver of set-off</b>	By acquiring any CCDS, each CCDS holder will be deemed to have waived any right of set-off or counterclaim that such CCDS holder might otherwise have against the Society in respect of or arising under the CCDS whether prior to or in a winding-up or dissolution.
<b>Redemption</b>	The CCDS will constitute permanent non-withdrawable deferred shares and will have no maturity date. The Society will have neither an obligation nor any right to redeem

or, save following a purchase as referred to in “*Purchases*” below, cancel the CCDS and the CCDS holders will not have any right to require the Society to redeem, purchase or cancel the CCDS.

**Purchases**                    The Society and its subsidiaries will be permitted, at any time, subject to the consent of or non-objection from the PRA if then required, purchase CCDS in the open market or otherwise at any price. CCDS so purchased may, at the option of the Society, be held, re-issued and/or re-sold or surrendered to the registrar for cancellation.

**Enforcement**                There will be no events of default in respect of the CCDS.

**Winding-Up, Amalgamation and Transfer of Business**                    On a winding-up or dissolution of the Society, the rights of the holders of Outstanding CCDS to participate in the winding-up or dissolution shall, save for declared and unpaid Distributions as provided in Condition 4.8, be limited to an entitlement to share in the Surplus following payment of all amounts in respect of Liabilities of the Society and any amounts payable pursuant to Condition 4.8 and claims ranking or expressed to rank *pari passu* therewith, provided that such entitlement shall be capped at the Average Principal Amount per CCDS.

On an amalgamation or transfer under section 93 or 94 of the Act, the CCDS shall become deferred shares in the Resulting Society, having such terms and conditions as are necessary to ensure that both the CCDS and any other deferred shares which, prior to such amalgamation or transfer, constituted Common Equity Tier 1 Capital of the other society, shall constitute Common Equity Tier 1 Capital of the Resulting Society.

On a transfer of business under section 97 of the Act, the Successor Entity will, as from the vesting date, assume a Subordinated Deposit to each holder of CCDS, which Subordinated Deposit shall be applied on the vesting date (or as soon as reasonably practicable thereafter), on behalf of the CCDS holder, in the subscription of such number of ordinary shares (which may or may not carry voting rights) in the Successor Entity or, if appropriate, any direct or indirect parent company of the Successor Entity, ranking *pari passu* in all respects with the then existing ordinary shares of such Successor Entity or such parent, as applicable, as have an aggregate market value immediately following such subscription as near as practicable to, but not less than, the market value of the CCDS immediately prior to the time of transfer of the business of the Society to the Successor Entity, as determined by an independent financial adviser.

**Distributions**                The Board may, in its sole and absolute discretion, from time to time declare Distributions in respect of the CCDS. With respect to any given financial year of the Society, the Board may declare an Interim Distribution during such financial year and/or a Final Distribution in respect of such financial year.

A Distribution (or any part thereof) may be declared unconditionally or subject to satisfaction of such conditions as the Board may determine.

If an Interim Distribution is declared during any financial year, it will (subject to satisfaction of the relevant conditions to payment, if any) be paid on 20 February (or, if such day is not a business day in London, the next following day which is a business day in London) in such financial year and if a Final Distribution is declared in respect of any financial year, it will (subject to satisfaction of the relevant conditions to payment, if any) be paid on 20 August (or, if such day is not a business day in London, the next following day which is a business day in London) falling in the financial year immediately following the financial year in respect of which the Final Distribution is declared.

The Society shall be entitled to change these expected payment dates for Interim Distributions and Final Distributions upon notice to the CCDS holders.

The Board shall have full discretion at all times whether or not to declare any Interim Distribution or Final Distribution, and (if declared) the amount of any such Distribution (subject to the Cap). Further, Distributions will be paid only out of available distributable items, and subject to any maximum distributable amount restrictions under Article 141 of CRD IV or any law or regulation implementing such Article.

No amount shall accrue in respect of Distributions, nor shall any amount accumulate if the Board does not declare any Distributions. Failure to declare any Distributions shall not constitute a default by the Society for any purpose.

**Cap on  
Distributions**

The total Distribution paid on each CCDS in respect of any given financial year of the Society shall not exceed the Cap.

Whilst the Board will not declare any Distributions in respect of the Society's financial year ending 31 March 2018, for illustrative purposes only the Cap on such Distributions, if declared, would be determined by applying the CPI annual inflation percentage published by the Office for National Statistics in its statistical bulletin for March 2018 to the prevailing Cap in respect of the financial year to 31 March 2017 of £15.42.

The Cap will be adjusted for inflation in each year in accordance with, and subject to, the Rules of the Society.

**Distribution  
Policy**

The Board intends to set the following Distribution Policy in respect of Distributions to be declared in respect of the CCDS. The Distribution Policy is entirely discretionary, and the Board may elect to amend or depart from such policy at any time.

When determining the interim or final Distributions (if any) to be declared in respect of the CCDS in respect of any given financial year, the Board will have regard to all relevant factors which it considers to be appropriate, including:

- the profitability of the Society and its resources available for distribution;
- the outlook for the Society's business, its short-term and long-term viability and the impact on the Society of the macro-economic environment in the UK, including inflation;
- the capital and liquidity position of the Society at the time of declaring the Distribution;
- the value to the Society of the capital provided by CCDS holders and rewarding investment in the capital of the Society in a commercially responsible manner, having regard to the risks inherent in such investments and the Society's need to maintain access to capital in the future;
- the benefits received by other members of the Society through the operation of the Society's business in accordance with the principles of mutuality; and
- the Cap on Distributions under the Society's Rules,

and subject always to applicable law and regulation and the following overriding fiduciary duties and principles:

- the duty of the directors to act in the best interests of the Society;
- the duty of the directors to have due regard to the interests of all categories of member, both current and future, of the Society; and
- the principles of mutuality that apply by virtue of being a building society.

The Board currently intends not to declare any Distributions in respect of the financial years ended 31 March 2018 and 31 March 2019.

The current intention of the Board is to target the payment of Distributions thereafter as follows:

- in respect of the financial year ended 31 March 2020, an Interim Distribution of £0.50 per CCDS paid in February 2020 and a Final Distribution of £0.50 per CCDS paid in August 2020;
- in respect of the financial year ended 31 March 2021, an Interim Distribution of £1.00 per CCDS paid in February 2021 and a Final Distribution of £1.00 per CCDS paid in August 2021;
- in respect of the financial year ended 31 March 2022, an Interim Distribution of £1.50 per CCDS paid in February 2022 and a Final Distribution of £1.50 per CCDS paid in August 2022; and
- in respect of the financial year ended 31 March 2023, an Interim Distribution of £2.25 per CCDS paid in February 2023 and a Final Distribution of £2.25 per CCDS paid in August 2023.

The Board currently intends, under normal circumstances, to adopt a stable distribution policy after the financial year ended 31 March 2023, and therefore expects that the Distribution level indicated above for the financial year ended 31 March 2023 would be appropriate for subsequent years, subject to the Society's then-current and anticipated financial position being viewed as satisfactory and any other factors considered by the Board to be relevant.

The Society notes, however, that the targeted path of Distributions and the targeted long-term Distributions set out above are dependent on improvement in the Society's annual profitability from its current level. In the event that the Society's profitability and/or financial position diverges from the Board's current expectations, it is likely that the Board will choose to amend its Distribution Policy or depart from it.

The indications stated above are not binding on the Society and the Board will have absolute discretion (subject to applicable law and regulation) whether or not to declare any interim or final Distribution in respect of any financial year and, if any such Distribution is declared, the amount of such Distribution. Accordingly, in respect of any given financial year, the Board may elect not to declare any Distributions, or may declare an interim and/or a final Distribution, and any such Distribution may be higher (subject to the Cap) or lower than the indications stated above. Further, the Board may amend its Distribution Policy at any time.

<b>Further issues</b>	The Society shall be at liberty from time to time, without any requirement to obtain consent from or afford pre-emption rights to the CCDS holders, to create and issue at any price further deferred shares that are consolidated and form a single series with the outstanding CCDS.
<b>Form</b>	<p>The CCDS will be issued in registered form and will upon issue be represented by a Global Certificate and will be deposited with, and registered in the name of a nominee for, a common depositary for the Clearing Systems.</p> <p>Beneficial interests in the CCDS may be traded in the Clearing Systems. Definitive certificates will not be printed unless the Clearing Systems close and there is no appropriate successor or alternative clearing system available.</p>
<b>Clearing Systems</b>	<p>Euroclear and Clearstream, Luxembourg.</p> <p>The CCDS have been registered with the International Security Identification Number (ISIN) GB00BYWR8Q80 and Common Code 179627256.</p>
<b>Voting Rights</b>	<p>At any meeting of the CCDS holders as a separate class, each CCDS holder shall have one vote for each CCDS held.</p> <p>At any general meeting of the members of the Society, any registered holder of any CCDS shall have a single vote (regardless of the number of CCDS held by it). However, for so long as the CCDS are traded in the Clearing Systems (which is expected to remain the case indefinitely), the only registered holder of CCDS shall be the nominee for the common depositary for the Clearing Systems, and the nominee will elect not to exercise that single vote, with the effect that investors in the CCDS will not be entitled to vote at general meetings of the Society.</p>
<b>Listing</b>	The Society expects to make an application for the CCDS to be admitted to trading on the Euro MTF market of the Luxembourg Stock Exchange and to be listed on the Official List of the Luxembourg Stock Exchange, with effect from on or around the date of issue of the CCDS.
<b>Governing Law</b>	The CCDS and any non-contractual obligations arising out of or in connection with the CCDS will be governed by, and construed in accordance with, English law.

## Overview of the Tier 2 Notes

<b>Issuer</b>	The Society.
<b>Securities</b>	11 per cent. Fixed Rate Subordinated Tier 2 Notes due 2038.
<b>Currency</b>	British pounds sterling (£).
<b>Issue Price</b>	100 per cent. of the principal amount.
<b>Status and Subordination</b>	<p>The Tier 2 Notes will constitute direct, unsecured and subordinated obligations of the Society and will rank <i>pari passu</i>, without any preference, among themselves.</p> <p>In a winding-up, claims in respect of the Tier 2 Notes will rank:</p> <ul style="list-style-type: none"> <li>(a) junior to claims in respect of unsubordinated obligations of the Society (including claims of depositors and claims of investing members of the Society as regards the principal and interest due on share investments (other than deferred share investments)), senior non-preferred obligations of the Society (if any) and any subordinated obligations of the Society not falling within (b) or (c) below;</li> <li>(b) at least <i>pari passu</i> with claims in respect of the Society's obligations which constitute, or would but for any applicable limitation on the amount of such capital constitute, tier 2 capital; and</li> <li>(c) in priority to claims in respect of obligations of the Society which constitute, or would but for any applicable limitation on the amount of such capital constitute, tier 1 capital and any other claims which rank or are expressed to rank junior to the claims in respect of the Tier 2 Notes (including claims in respect of the PIBS and the CCDS).</li> </ul>
<b>Waiver of set-off</b>	Subject to applicable law, no holder of Tier 2 Notes will be entitled to exercise, claim or plead any right of set-off, compensation or retention in respect of any amount owed to it by the Society arising under or in connection with the Tier 2 Notes and each holder shall be deemed to have waived all such rights of set-off, compensation or retention.
<b>Interest</b>	The Tier 2 Notes will bear interest on their principal amount at the rate of 11 per cent. per annum, payable in equal instalments semi-annually in arrear on 12 April and 12 October in each year, commencing on 12 October 2018.
<b>Maturity</b>	Unless previously redeemed or purchased and cancelled, the Society will redeem the Tier 2 Notes at their principal amount together with accrued and unpaid interest on 12 April 2038.
<b>Early Redemption at the Option of the Society</b>	The Society will be entitled, in its sole discretion but subject to the conditions set out under " <i>Conditions to Redemption and Purchase</i> " below, to redeem all (but not some only) of the Tier 2 Notes on 12 April 2033 or any Interest Payment Date thereafter at their principal amount, together with any accrued and unpaid interest up to (but excluding) the redemption date.
<b>Redemption following a Capital</b>	The Society will be entitled, in its sole discretion but subject to the conditions set out under " <i>Conditions to Redemption and Purchase</i> " below, to redeem all (but not some only) of the Tier 2 Notes at any time following the occurrence of a Tax Event or a

<b>Disqualification Event or a Tax Event</b>	<p>Capital Disqualification Event, at their principal amount together with any accrued and unpaid interest up to (but excluding) the redemption date.</p> <p>A <b>Tax Event</b> will be deemed to have occurred if, as a result of a change in tax law after the issue date of the Tier 2 Notes:</p> <ul style="list-style-type: none"> <li>• in making any payments on the Tier 2 Notes, the Society has paid or will or would on the next payment date be required to pay additional amounts (as described under “<i>Taxation</i>” below);</li> <li>• the Society is no longer, or will no longer be, entitled to claim a deduction in respect of any payments in respect of the Tier 2 Notes in computing its taxation liabilities or the amount of such deduction is or will be materially reduced;</li> <li>• the Tier 2 Notes are, or will be, prevented from being treated as loan relationships for United Kingdom tax purposes; or</li> <li>• the Society is not, or will not be, able to have losses or deductions set against any profits or gains, or profits or gains offset by any losses or deductions, of companies with which it is or would otherwise be so grouped for applicable United Kingdom tax purposes (whether under the group relief system current as at the date of issue of the Tier 2 Notes or any similar system or systems having like effect as may from time to time exist).</li> </ul> <p>A <b>Capital Disqualification Event</b> will be deemed to have occurred if there is a change (which has occurred or which the PRA considers to be sufficiently certain) in the regulatory classification of the Tier 2 Notes which becomes effective after the date of issue of the Tier 2 Notes and that results, or would be likely to result, in the entire principal amount of the Tier 2 Notes or any part thereof being excluded from the tier 2 capital of the Society (whether on an individual or consolidated basis).</p>
<b>Purchases</b>	<p>The Society and its subsidiaries may, at their option but subject as provided under “<i>Conditions to Redemption and Purchase</i>” below, purchase (or otherwise acquire) any of the outstanding Tier 2 Notes at any price in the open market or otherwise at any time.</p>
<b>Conditions to Redemption and Purchase</b>	<p>Any redemption or purchase of the Tier 2 Notes prior to their maturity will be subject to obtaining the permission of the PRA and to compliance with prevailing prudential rules.</p>
<b>Enforcement</b>	<p>Enforcement events in respect of the Tier 2 Notes will be limited to instituting proceedings for the winding-up of the Society in England if it fails to pay any amounts when due in respect of the Tier 2 Notes and/or proving in a winding-up of the Society (such claim being subordinated as provided above).</p>
<b>Form</b>	<p>The Tier 2 Notes will be issued in registered form and will upon issue be represented by a Global Certificate and will be deposited with, and registered in the name of a nominee for, a common depositary for the Clearing Systems.</p> <p>Beneficial interests in the Tier 2 Notes may be traded in the Clearing Systems. Definitive certificates will not be printed unless the Clearing Systems close and there is no appropriate successor or alternative clearing system available.</p>
<b>Denominations</b>	<p>£1,000 and integral multiples of £100 in excess thereof.</p>

<b>Taxation</b>	All payments in respect of the Tier 2 Notes will be made without deduction for or on account of UK withholding taxes, unless required by law. In the event that any such deduction is required to be made in respect of payments of interest (but not principal), the Society will, save in certain limited circumstances, be required to pay additional amounts to cover the amounts so deducted.
<b>Clearing Systems</b>	<p>Euroclear and Clearstream, Luxembourg.</p> <p>The Tier 2 Notes have been registered with the International Security Identification Number (ISIN) XS1775405795 and Common Code 177540579.</p>
<b>Listing</b>	The Society expects to make an application for the Tier 2 Notes to be admitted to trading on the Euro MTF market of the Luxembourg Stock Exchange and listed on the Official List of the Luxembourg Stock Exchange, with effect from on or around the date of issue of the Tier 2 Notes.
<b>Governing Law</b>	The Tier 2 Notes and any non-contractual obligations arising out of or in connection with the Tier 2 Notes will be governed by, and construed in accordance with, English law.



### PART III – INCORPORATION BY REFERENCE

The following documents have previously been published or are published simultaneously with these Listing Particulars and have been filed with the Luxembourg Stock Exchange and shall be deemed to be incorporated in, and form part of, these Listing Particulars:

- (1) the Society's audited consolidated financial statements as of and for the financial year ended 31 March 2017 (including the notes thereto), and the auditors' report thereon (the **2017 Financial Statements**);
- (2) the Society's audited consolidated financial statements as of and for the financial year ended 31 March 2016 (including the notes thereto), and the auditors' report thereon (the **2016 Financial Statements**);
- (3) the Society's audited consolidated financial statements as of and for the financial year ended 31 March 2015 (including the notes thereto), and the auditors' report thereon (the **2015 Financial Statements** and, together with the 2017 Financial Statements and the 2016 Financial Statements, the **Consolidated Historical Financial Statements**);
- (4) certain additional information identified below, incorporated by reference from the Society's Annual Report and Accounts for each of the years ended 31 March 2015, 2016 and 2017;
- (5) the Society's unaudited interim condensed consolidated financial statements as of and for the 6 month period ended 30 September 2017 (including the notes thereto) (the **H1 2017/8 Interim Financial Statements**);
- (6) the announcements made by the Society on 13 December 2017 (the **December Announcement**), 8 March 2018 (the **Launch Announcement**) and 10 April 2018 (the **Results Announcement**) relating to the LME; and
- (7) the consent and exchange offer memorandum dated 8 March 2018 prepared by the Society in relation to the Exchange Offers (the **Consent and Exchange Offer Memorandum**).

The Society will provide, without charge, to each person to whom a copy of these Listing Particulars have been delivered, upon the request of such person, an electronic copy of any or all of the documents deemed to be incorporated herein by reference. Written requests for such documents should be directed to Treasury at West Bromwich Building Society, 2 Providence Place, West Bromwich, B70 8AF. In addition, copies of these Listing Particulars and each document incorporated by reference herein are available on the website of the Luxembourg Stock Exchange (<http://www.bourse.lu>).

The table below sets out the relevant page references for the Consolidated Historical Financial Statements and the H1 2017/8 Interim Financial Statements.

#### H1 2017/8 Interim Financial Statements

	H1 2017/8 Interim Financial Statements page reference
Income statement .....	6
Statement of comprehensive income .....	7
Statements of Financial Position .....	8
Statements of Changes in Members' Interest .....	9-10
Cash flow statement.....	11-12
Notes to the consolidated annual financial statements.....	13-24

## 2017 Financial Statements

	Annual Report and Accounts 2017 page reference
Independent Auditors' Report .....	47
Income statement .....	48
Statement of comprehensive income .....	49
Statements of Financial Position .....	50
Statements of Changes in Members' Interest .....	51-52
Cash flow statement.....	53-54
Notes to the consolidated annual financial statements.....	55-110

In addition, the Business Review section included from pages 8-28 in the Society's Annual Report and Accounts 2017 form part of the 2017 Financial Statements.

## 2016 Financial Statements

	Annual Report and Accounts 2016 page reference
Independent Auditors' Report .....	39
Income statement .....	40
Statement of comprehensive income .....	41
Statements of Financial Position .....	42
Statements of Changes in Members' Interest .....	43
Cash flow statement.....	45
Notes to the consolidated annual financial statements.....	47-102

In addition, the Business Review section included from pages 5-18 in the Society's Annual Report and Accounts 2016 form part of the 2016 Financial Statements.

## 2015 Financial Statements

	Annual Report and Accounts 2015 page reference
Independent Auditors' Report .....	40
Income statement .....	41
Statement of comprehensive income .....	42
Statements of Financial Position .....	43
Statements of Changes in Members' Interest .....	44
Cash flow statement.....	46
Notes to the consolidated annual financial statements.....	48-102

In addition, the Strategic Review section included elsewhere the Society's Annual Report and Accounts 2015 form part of the 2015 Financial Statements.

Any non-incorporated parts of a document referred to herein are either deemed not relevant for an investor or are otherwise covered elsewhere in these Listing Particulars.

Any documents themselves incorporated by reference in the documents incorporated by reference in these Listing Particulars shall not form part of these Listing Particulars.

## **PART IV – DIRECTORS, PRINCIPAL AND HEAD OFFICE AND ADVISERS**

### **Directors**

Mark Nicholls	Chairman and Non-Executive Director
Jonathan Westhoff	Chief Executive
Ashraf Piranie	Group Finance & Operations Director
Martin Ritchley	Deputy Chairman, Senior Independent Director and Non-Executive Director
Julie Hopes	Non-Executive Director
Mark Preston	Non-Executive Director
Richard Sommers	Non-Executive Director
Colin Walklin	Non-Executive Director
James Turner	Non-Executive Director

Principal Office and Head Office	Head Office 2 Providence Place West Bromwich B70 8AF United Kingdom Tel: +44 (0) 345 241 3784
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English Law Advisers to the Society	Allen & Overy LLP One Bishops Square London E1 6AD United Kingdom
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Financial Adviser to the Society	Evercore Partners International LLP 15 Stanhope Gate London W1K 1LN United Kingdom
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Registrar	Citibank N.A., London Branch 6th floor, Citigroup Centre Canary Wharf London E14 5LB United Kingdom
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## PART V – REASONS FOR OFFER, USE OF PROCEEDS AND CCDS DISTRIBUTION POLICY

### 1. REASONS FOR THE OFFER

In common with other financial institutions, the Society is required by law to maintain certain levels of capital to absorb losses. The Society's regulatory capital mainly comprises retained profit which has been built up over many years. From time to time, the Society has also issued capital instruments to external investors, including the Society's 3,650 Profit Participating Deferred Shares (the **PPDS**) and £75 million 6.15 per cent. Permanent Interest Bearing Shares (the **PIBS**).

The Society offered the Securities as part of exchange offers (the **Exchange Offers**) available to eligible professional investors holding its PPDS and PIBS, as more fully described in the Consent and Exchange Offer Memorandum. In particular, the Society invited eligible professional investors holding PPDS to offer to exchange their PPDS for a combination of CCDS, Tier 2 Notes and cash, and invited eligible professional investors holding PIBS to offer to exchange their PIBS for a combination of CCDS and cash.

The reason for the Exchange Offers, as more fully set out in the Consent and Exchange Offer Memorandum, is to enable the Society to modernise its capital structure following the implementation of the new prudential regimes under CRD IV and CRR, which were introduced following the issue of the PPDS and the PIBS, and to maintain its capital at prudent levels having regard to its present and anticipated future capital requirements.

The CCDS will constitute Common Equity Tier 1 capital – the highest quality form of capital available to building societies – and the Tier 2 Notes will constitute Tier 2 capital.

### 2. USE OF PROCEEDS

Since the CCDS and the Tier 2 Notes are being issued in exchange for existing capital instruments rather than new money investment, there will be no cash proceeds generated by the issue of the CCDS and the Tier 2 Notes.

### 3. DISTRIBUTION POLICY IN RESPECT OF THE CCDS

The Society's Board of Directors (the **Board**) intends to set the following policy (the **Distribution Policy**) in respect of periodic distributions (**Distributions**) to be declared in respect of the CCDS. The Distribution Policy is entirely discretionary, and the Board may elect to amend or depart from such policy at any time.

When determining the interim or final Distributions (if any) to be declared in respect of the CCDS in respect of any given financial year, the Board will have regard to all relevant factors which it considers to be appropriate, including:

- the profitability of the Society and its resources available for distribution;
- the outlook for the Society's business, its short-term and long-term viability and the impact on the Society of the macro-economic environment in the UK, including inflation;
- the capital and liquidity position of the Society at the time of declaring the Distribution;
- the value to the Society of the capital provided by CCDS holders and rewarding investment in the capital of the Society in a commercially responsible manner, having regard to the risks inherent in such investments and the Society's need to maintain access to capital in the future;

- the benefits received by other members of the Society through the operation of the Society's business in accordance with the principles of mutuality; and
- the Cap on Distributions under the Society's Rules,

and subject always to applicable law and regulation and the following overriding fiduciary duties and principles:

- the duty of the directors to act in the best interests of the Society;
- the duty of the directors to have due regard to the interests of all categories of member, both current and future, of the Society; and
- the principles of mutuality that apply by virtue of being a building society.

The Board currently intends not to declare any Distributions in respect of the financial years ended 31 March 2018 and 31 March 2019.

The current intention of the Board is to target the payment of Distributions thereafter as follows:

- in respect of the financial year ended 31 March 2020, an Interim Distribution of £0.50 per CCDS paid in February 2020 and a Final Distribution of £0.50 per CCDS paid in August 2020;
- in respect of the financial year ended 31 March 2021, an Interim Distribution of £1.00 per CCDS paid in February 2021 and a Final Distribution of £1.00 per CCDS paid in August 2021;
- in respect of the financial year ended 31 March 2022, an Interim Distribution of £1.50 per CCDS paid in February 2022 and a Final Distribution of £1.50 per CCDS paid in August 2022; and
- in respect of the financial year ended 31 March 2023, an Interim Distribution of £2.25 per CCDS paid in February 2023 and a Final Distribution of £2.25 per CCDS paid in August 2023.

The Board currently intends, under normal circumstances, to adopt a stable distribution policy after the financial year ended 31 March 2023, and therefore expects that the Distribution level indicated above in respect of the financial year ended 31 March 2023 would be appropriate for subsequent years, subject to the Society's then-current and anticipated financial position being viewed as satisfactory and any other factors considered by the Board to be relevant.

The Society notes, however, that the targeted path of Distributions and the targeted long-term Distributions set out above are dependent on improvement in the Society's annual profitability from its current level. In the event that the Society's profitability and/or financial position diverges from the Board's current expectations, it is likely that the Board will choose to amend its Distribution Policy or depart from it.

The indications stated above are not binding on the Society and the Board will have absolute discretion (subject to applicable law and regulation) whether or not to declare any Interim Distribution or Final Distribution in respect of any financial year and, if any such Distribution is declared, the amount of such Distribution. Accordingly, in respect of any given financial year, the Board may elect not to declare any Distributions, or may declare an Interim Distribution and/or a Final Distribution, and any such Distribution may be higher (subject to the Cap on Distributions under the Society's Rules) or lower than the indications stated above.

## **PART VI – PRESENTATION OF INFORMATION**

### **1. GENERAL**

**Investors should rely only on the information in these Listing Particulars. No person has been authorised to give any information or to make any representations other than those contained in these Listing Particulars in connection with the offer of the Securities and, if given or made, such information or representations must not be relied upon as having been authorised by or on behalf of the Society or any of its directors, officers, employees, agents or affiliates. Without prejudice to any obligation of the Society under law or the rules of the Luxembourg Stock Exchange to publish further information on the website of the Luxembourg Stock Exchange, neither the delivery of these Listing Particulars nor any sale of Securities shall, under any circumstances, create any implication that there has been no change in the business or affairs of the Society since the date hereof or that the information contained herein is correct as of any time subsequent to its date.**

The contents of these Listing Particulars are not to be construed as legal, business or tax advice. Each prospective investor should consult his or her own lawyer, financial adviser or tax adviser for legal, financial or tax advice in relation to any subscription, purchase or proposed subscription or purchase of Securities.

None of the Society or any of its directors, officers, employees, agents or affiliates makes any representation to any prospective investor regarding the legality of an investment by such investor.

Neither these Listing Particulars nor any other information supplied in connection with the issue of the Securities is intended to provide the basis of any credit or other valuation and should not be considered as a recommendation by the Society or any of its directors, officers, employees, agents or affiliates that any recipient of either these Listing Particulars, or of any other information supplied in connection with these Listing Particulars or the issue of the Securities, should purchase any Securities. Each investor must make its own independent investigation of the financial condition and affairs, and its own appraisal of the creditworthiness, of the Society and of the rights attaching to the Securities. The provision of these Listing Particulars and related materials does not constitute an offer or invitation by or on behalf of the Society to subscribe for or to purchase any Securities.

### **2. PRESENTATION OF FINANCIAL INFORMATION**

Prospective investors should consult their own professional advisers to gain an understanding of the financial information contained in these Listing Particulars. An overview of the basis for presentation of financial information in these Listing Particulars is set out below.

#### **Consolidated Historical Financial Statements**

These Listing Particulars incorporate by reference the Society's 2017 Financial Statements, 2016 Financial Statements and 2015 Financial Statements (together, the Consolidated Historical Financial Statements) and its H1 2017/8 Interim Financial Statements.

The Consolidated Historical Financial Statements and the H1 2017/8 Interim Financial Statements have been prepared in accordance with IFRS.

The Consolidated Historical Financial Statements have each been audited, without qualification, by KPMG, independent auditors, in accordance with International Standards on Auditing (UK & Ireland) issued by the Auditing Practices Board in the UK. The H1 2017/8 Interim Financial Statements are unaudited.

Prospective investors should be aware that IFRS and generally accepted accounting procedures in the UK (**UK GAAP**) differ from each other in certain significant respects. The Consolidated Historical Financial Statements have not been prepared in accordance with UK GAAP, nor has the Society prepared a reconciliation or quantification of differences between IFRS and UK GAAP.

The Society publishes its annual report and results and its half-year interim statement each year. These can be obtained on the Society's website ([www.westbrom.co.uk](http://www.westbrom.co.uk)).

### **Unaudited financial information**

Certain financial information in these Listing Particulars comprises unaudited financial information which has been extracted without material adjustment from the accounting records of the Society including the H1 2017/8 Interim Financial Statements. In particular, financial information included within "*Part XVIII: Selected Statistical Information*" is unaudited and has been extracted from the Society's management information systems.

## **3. CURRENCIES**

Unless otherwise indicated, in these Listing Particulars, all references to:

- **euro** or **€** are to the lawful currency of the European Union (as adopted by certain member states); and
- **pounds sterling, sterling** or **£** are to the lawful currency of the UK.

Unless otherwise indicated, the financial information contained in these Listing Particulars has been expressed in pounds sterling. The Society's functional currency is pounds sterling and the Society prepares its financial statements in pounds sterling.

## **4. FORWARD-LOOKING STATEMENTS**

Certain information contained or incorporated by reference in these Listing Particulars including any information as to the Society's strategy, plans or future financial or operating performance constitute "forward-looking statements". These forward-looking statements can be identified by the use of forward-looking terminology, including the terms "believes", "estimates", "anticipates", "projects", "expects", "intends", "aims", "plans", "predicts", "may", "will", "seeks" or "should" or, in each case, their negative or other variations or comparable terminology, or by discussions of strategy, plans, objectives, goals, future events or intentions. These forward-looking statements include all matters that are not historical facts. They appear in a number of places throughout these Listing Particulars and include statements regarding the intentions, beliefs or current expectations of the Society concerning, amongst other things: the Society's results of operations, financial condition, prospects, growth, strategies and the industry in which the Society operates.

By their nature, forward-looking statements involve risks and uncertainties because they relate to events and depend on circumstances that may or may not occur in the future. Forward-looking statements are not guarantees of future performance. The Society's actual results of operations, financial condition, and the development of the financial services industry in which the Society operates, may differ materially from those suggested by the forward-looking statements contained in these Listing Particulars. In addition, even if the Society's results of operations, financial condition, and the development of the financial services industry are consistent with the forward-looking statements contained in these Listing Particulars, those results or developments may not be indicative of results or developments in subsequent periods.

Prospective investors are advised to read, in particular, "*Part I: Risk Factors*", "*Part XII: Description of the Society's Business*" and "*Part XVI: Operating and Financial Review*" as well as the

Consolidated Historical Financial Statements and H1 2017/8 Interim Financial Statements incorporated by reference in this document for a more complete discussion of the factors that could affect the Society's future performance and the financial services industry. Forward-looking statements and other statements contained in these Listing Particulars regarding matters that are not historical facts involve predictions. No assurance can be given that such future results will be achieved; actual events or results may differ materially as a result of risks and uncertainties facing the Society. In light of these risks, uncertainties and assumptions, the events described in the forward-looking statements in these Listing Particulars may not occur.

The forward-looking statements contained in these Listing Particulars speak only as of the date of these Listing Particulars. The Society and the Directors expressly disclaim any obligation or undertaking to update or revise publicly any forward-looking statements, whether as a result of new information, future events or otherwise, unless required to do so by applicable law. All subsequent written and oral forward-looking statements attributable to the Group or individuals acting on behalf of the Group are expressly qualified in their entirety by this paragraph.

## **5. MARKET, ECONOMIC AND INDUSTRY DATA**

The Listing Particulars contain information regarding the Society's business and the industry in which it operates and competes, which the Society has obtained from third-party sources.

The Society and other institutions operating in the financial services industry make available a wide range of financial and operational information to regulatory and market bodies, including the BoE and UK Finance. These bodies use certain of the data supplied to publish market share statistics relating to retail mortgage lending and savings, among other matters. However, no assurance can be made that the information reported to these bodies by different market participants is, in all cases, directly comparable.

In some cases, independently determined industry data is not available. In these cases, any Society market share included in these Listing Particulars is referred to as having been estimated. All such estimates have been made by the Society using its own information and other market information which is publicly available. All such estimations have been made in good faith based on the information available and the Society's knowledge of the market within which it operates.

Where third-party information has been used in these Listing Particulars, the source of such information has been identified. In the case of the presented economic and statistical information, similar information may be obtainable from other sources, although the underlying assumptions and methodology, and consequently the resulting data, may vary from source to source.

The Society confirms that all information extracted from third party sources has been accurately reproduced and, as far as the Society is aware and has been able to ascertain from information published by those sources, no facts have been omitted which would render the reproduced information inaccurate or misleading. Where third party information has been used in these Listing Particulars, the source of such information has been identified.

Where information has not been independently sourced, it is the Society's own information.

## **6. NO INCORPORATION OF WEBSITE INFORMATION**

The Society's website is [www.westbrom.co.uk](http://www.westbrom.co.uk). The information on this website or any website mentioned in these Listing Particulars or any website directly or indirectly linked to these websites has not been verified and, save in respect of any information specifically incorporated by reference in this document which also appears on the Society's website, is not incorporated by reference into these Listing Particulars and investors should not rely on it.



## **7. DEFINITIONS**

Certain capitalised and other terms used in these Listing Particulars are defined in “*Part XXIII: Definitions*”.

## **8. ROUNDING**

Certain figures contained in these Listing Particulars, including financial information, may have been subject to rounding adjustments. Accordingly, in certain instances, the sum of the numbers in a column or a row in tables contained in these Listing Particulars may not conform exactly to the total figure given for that column or row. Percentages in tables have been rounded and accordingly may not add up to 100 per cent. Where the figure “0” appears in a table it means that the relevant item has been rounded to zero. Where a “—” appears in a table, it means that there is no figure for the relevant item.

## **9. BUILDING SOCIETIES AND BANKS**

For a discussion of certain key differences between UK building societies and banks, see “*Part XI: - Industry Overview*”.

## **10. CREDIT RATING AGENCIES**

These Listing Particulars contain references to Moody’s, Fitch and S&P.

Each of Moody’s, S&P and Fitch is established in the European Union and is registered under the CRA Regulation. A credit rating is not a recommendation to buy, sell or hold securities and may be subject to revision, suspension or withdrawal at any time by the assigning rating organisation.

## PART VII – DISTRIBUTION, SETTLEMENT AND TRANSFERS

### 1. DISTRIBUTION

As noted under “*Part V – Reasons for Offer and Use of Proceeds*”, the Securities have been offered only as part of Exchange Offers available to eligible professional investors holding the Society’s PPDS and PIBS. The Exchange Offers were subject to offer restrictions set out in the Consent and Exchange Offer Memorandum, including in the United States, Australia, South Africa, Japan, Hong Kong, Singapore, Italy, Switzerland and Canada. See also “*Selling Restrictions*” below.

Furthermore, the Society intends that the Securities should not at any time (upon initial issue or otherwise) be offered, sold or otherwise made available to retail investors, and should only be made available to persons satisfying all of the following criteria:

- (1) a person that, if such person were receiving services in the course of a firm carrying on a regulated activity, would be a client who is either a ‘professional client’ or an ‘eligible counterparty’ under MiFID II;
- (2) a ‘qualified investor’ within the meaning of Article 2(1)(e) of Directive 2003/71/EC, as amended; and
- (3) if it is in the UK, it is an ‘investment professional’ for the purposes of Article 19 of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005.

### 2. RESTRICTIONS ON MARKETING AND SALES TO RETAIL INVESTORS

**MiFID II product governance / professional investors and ECPs only target market** – Solely for the purposes of the manufacturer’s product approval process, the target market assessment in respect of the Securities has led to the conclusion that: (i) the target market of the Securities is ‘eligible counterparties’ and ‘professional clients’ only, each as defined in MiFID II; and (ii) all channels for the distribution of the Securities to eligible counterparties and professional clients are appropriate. Any person subsequently offering, selling or recommending the Securities (a **distributor**) should take into consideration the manufacturer’s target market assessment; however, a distributor subject to MiFID II is responsible for undertaking its own target market assessment in respect of the Securities (by either adopting or refining the manufacturer’s target market assessment) and determining appropriate distribution channels.

**PRIIPs Regulation / prohibition of sales to EEA retail investors** – The Securities are not intended to be offered, sold or otherwise made available to and should not be offered, sold or otherwise made available to any retail investor in the European Economic Area (**EEA**). For these purposes, a **retail investor** means a person who is one (or more) of: (i) a ‘retail client’ as defined in point (11) of MiFID II; or (ii) a customer within the meaning of Directive 2002/92/EC, where that customer would not qualify as a ‘professional client’ as defined in point (10) of Article 4(1) of MiFID II. No key information document required by Regulation (EU) No 1286/2014 (the **PRIIPs Regulation**) for offering or selling securities falling within scope of the PRIIPs Regulation or otherwise making them available to retail investors in the EEA has been prepared and therefore offering or selling the Securities or otherwise making them available to any retail investor in the EEA may, if the Securities were to be determined to fall within the scope of the PRIIPs Regulation, be unlawful under the PRIIPs Regulation.

**COBS 22.2 / restriction on marketing and sales to retail investors** - The Securities are financial instruments with complex features, and will not be a suitable or appropriate investment for all investors. The offer, sale or distribution of the Securities to certain investors, including retail investors, may be restricted or prohibited by law in certain jurisdictions. In particular, in June 2015, the UK

Financial Conduct Authority (the **FCA**) published the Product Intervention (Contingent Convertible Instruments and Mutual Society Shares) Instrument 2015, which took effect from 1 October 2015 (the **Product Intervention Instrument**). Under the rules contained in the Product Intervention Instrument and Chapter 22.2 of the Conduct of Business Sourcebook (**COBS 22.2**) in the FCA's Handbook (as such rules may be amended or replaced from time to time, the **Product Intervention Rules**), there are restrictions on the sale of 'mutual society shares' (which would include the CCDS) to 'retail clients' in the EEA. For these purposes, a **retail client** is a person who is, or who if he were receiving services in the course of a firm carrying on a regulated activity would be, a client who is neither a 'professional client' nor an 'eligible counterparty' under MiFID II. Such restrictions may, absent an applicable exemption and depending on the nature of the relevant transaction with the retail client, require (amongst other things) the provision to the retail client of prescribed risk warnings, obtaining from the retail client certain confirmations and signed statements relating to the investment, limits on the amount of investments relative to a retail client's net assets and an assessment of whether the investment in the mutual society share is appropriate for the retail client.

The Society is required to comply with the Product Intervention Rules and COBS 22.2. Given the nature of the restrictions contained in the Product Intervention Instrument and COBS 22.2, the offer of CCDS described in these Listing Particulars is not made to retail clients (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2), and the Society will not offer or sell CCDS to retail clients, nor will the Society at any time take, or be required to take, any action which would facilitate an offer or sale of any CCDS to any retail client. By purchasing, or making or accepting an offer to purchase, any CCDS (or a beneficial interest therein) from the Society, each prospective investor represents, warrants, agrees with, and undertakes to, the Society that:

1. it is not a 'retail client' (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA;
2. whether or not it is subject to the Product Intervention Rules, it will not:
  - (A) sell or offer the CCDS (or any beneficial interest therein) to retail clients (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA; or
  - (B) communicate (including the distribution of these Listing Particulars) or approve an invitation or inducement to participate in, acquire or underwrite the CCDS (or any beneficial interests therein) where that invitation or inducement is addressed to or disseminated in such a way that it is likely to be received by a retail client (as that term is defined for the purposes of the Product Intervention Rules and COBS 22.2) in the EEA,

in any such case other than:

- (i) in relation to any sale or offer to sell CCDS (or any beneficial interest therein) to a retail client in or resident in the United Kingdom (the **UK**), in circumstances that do not and will not give rise to a contravention of the applicable Product Intervention Rules or COBS 22.2 by any person; and/or
- (ii) in relation to any sale or offer to sell CCDS (or any beneficial interest therein) to a retail client in any EEA member state other than the UK, where (a) it has conducted an assessment and concluded that (1) the relevant retail client understands the risks of an investment in the CCDS (or such beneficial interest therein), including if appropriate through the provision of appropriate risk warnings and the obtaining of all appropriate confirmations and statements from the retail client, and (2) the relevant retail client is able to bear the potential losses involved in an investment in the CCDS and (b) it has at all times acted in relation to such sale or offer in compliance with

MiFID II to the extent it applies to it or, to the extent MiFID II does not apply to it, in a manner which would be in compliance with MiFID II if it were to apply to it; and

3. it will at all times comply with all applicable laws, regulations and regulatory guidance (whether inside or outside the EEA) relating to the promotion, offering, distribution and/or sale of the CCDS (and any beneficial interest therein), including (without limitation) any such laws, regulations and regulatory guidance relating to determining the appropriateness and/or suitability of an investment in the CCDS (or any beneficial interest therein) by investors in any relevant jurisdiction.

Where acting as agent on behalf of a disclosed or undisclosed client when purchasing, or making or accepting an offer to purchase, any CCDS (or any beneficial interest therein) from the Society, the foregoing representations, warranties, agreements and undertakings will be given by and be binding upon both the agent and its underlying client.

### **3. SELLING RESTRICTIONS**

#### **General**

The distribution of these Listing Particulars and the offering and sale of Securities in certain jurisdictions may be restricted by law and therefore persons into whose possession these Listing Particulars come should inform themselves about and observe any such restrictions, including those in the paragraphs that follow. These Listing Particulars should not be distributed, and no offer or sale of the Securities will be made, in the United States, Australia, South Africa, Japan, Hong Kong, Singapore, Italy, Switzerland and Canada. Any failure to comply with applicable restrictions may constitute a violation of the securities laws of any such jurisdiction. No action has been taken or will be taken in any jurisdiction that is intended to permit a public offering or sale of the Securities, or possession or distribution of these Listing Particulars or any other offering or publicity material relating to the Securities, in any country or jurisdiction where action for that purpose is required.

None of the Securities may be offered for subscription, sale, purchase or delivery, or be subscribed, sold, purchased or delivered, and these Listing Particulars and any other offering material in relation to the Securities may not be circulated, in any jurisdiction where to do so would breach any securities laws or regulations of that jurisdiction or give rise to an obligation to obtain any consent, approval or permission, or to make any application, filing or registration.

The offer restrictions contained in this “Part V: *Distribution, Settlement and Transfers*”, including section 2 above and this section 3, are cumulative. Accordingly, any prospective investor in the Securities must be eligible to acquire the Securities in compliance with all such restrictions.

#### **United Kingdom**

Dealings in the Securities shall comply with all applicable provisions of FSMA with respect to anything done by any party in relation to the Securities in, from or otherwise involving the UK.

Any invitation or inducement to engage in investment activity (within the meaning of Section 21 of FSMA) in connection with the issue or sale of the Securities has only been communicated or caused to be communicated and will only be communicated or caused to be communicated in the UK in circumstances in which Section 21(1) of FSMA would not, if the Society was not an authorised person, apply to the Society. The Society does not intend the Securities to be offered or sold to persons in the United Kingdom unless they are persons who have professional experience in matters relating to investments falling within Article 19(5) of the Financial Services and Markets Act 2000 (Financial Promotion) Order 2005.

## **United States of America**

None of the Securities have been or will be registered under the Securities Act or the securities laws of any state or other jurisdiction in the United States and the Securities may not be offered or sold within the United States. Accordingly, the Securities may be offered and sold only outside the United States in reliance on Regulation S. Terms used in this paragraph have the meanings given to them under Regulation S under the Securities Act.

## **Belgium**

An offering of the Securities may not be advertised to any individual in Belgium qualifying as a consumer within the meaning of Article I.1 of the Belgian Code of Economic Law, as amended from time to time (a **Belgian Consumer**) and the Securities have not been offered, sold or resold, transferred or delivered, and will not be offered, sold, resold, transferred or delivered, and these Listing Particulars or any similar documents in relation to the Securities have not been distributed, and will not be distributed, directly or indirectly, to any Belgian Consumer.

## **Japan**

The Securities have not been and will not be registered under the Financial Instruments and Exchange Act of Japan (Law No. 25 of 1948, as amended) (the **FIEA**). The Securities may not be offered or sold directly or indirectly, in Japan or to, or for the benefit of, any resident in Japan (which term as used herein means any person resident in Japan, including any corporation or other entity organised under the laws of Japan), or to others for reoffering or resale, directly or indirectly, in Japan or to, or for the benefit of, a resident of Japan except pursuant to an exemption from the registration requirements of, and otherwise in compliance with, the FIEA and any other applicable laws, regulations and ministerial guidelines of Japan.

## **Australia**

No prospectus or other disclosure document (as defined in the Corporations Act 2001 of Australia (**Corporations Act**)) in relation to the Securities has been or will be lodged with the Australian Securities and Investments Commission (**ASIC**). Prospective investors should note that:

- (a) the Securities have not been and will not be (directly or indirectly) offered for issue or sale and no invitation, applications for issue, or offers to purchase, the Securities in, to or from Australia (including an offer or invitation which is received by a person in Australia) has been or will be made; and
- (b) these Listing Particulars, any information memorandum, advertisement or other offering material relating to the Securities, have not been and will not be distributed or published, in Australia,

unless (1) the aggregate consideration payable by each offeree or invitee is at least AUD500,000 (or its equivalent in other currencies, disregarding moneys lent by the offeror or its associates) or the offer or invitation otherwise does not require disclosure to investors in accordance with Part 6D.2 or Part 7.9 of the Corporations Act, (2) the offer or invitation is not made to a person who is a “retail client” within the meaning of section 761G of the Corporations Act, (3) such action complies with all applicable laws, regulations and directives and (4) such action does not require any document to be lodged with ASIC.

## **Hong Kong**

No Securities have been offered or sold or will be offered or sold in Hong Kong, by means of any document, other than (a) to “professional investors” as defined in the Securities and Futures Ordinance (Cap. 571) of Hong Kong (the **SFO**) and any rules made under the SFO; or (b) in other circumstances

which do not result in the document being a “prospectus” as defined in the Companies (Winding Up and Miscellaneous Provisions) Ordinance (Cap. 32) of Hong Kong (the **C(WUMP)O**) or which do not constitute an offer to the public within the meaning of the C(WUMP)O. No advertisement, invitation or document relating to the Securities has been issued or has been in the possession of any person for the purposes of issue, nor will any such advertisement, invitation or document be issued or be in the possession of any person for the purpose of issue, whether in Hong Kong or elsewhere, which is directed at, or the contents of which are likely to be accessed or read by, the public of Hong Kong (except if permitted to do so under the securities laws of Hong Kong) other than with respect to Securities which are or are intended to be disposed of only to persons outside Hong Kong or only to “professional investors” as defined in the SFO and any rules made under the SFO.

## **Italy**

The Securities are not being offered, directly or indirectly, in the Republic of Italy. None of these Listing Particulars or any other document or materials relating to the Securities have been or will be submitted to the clearance procedures of the *Commissione Nazionale per le Società e la Borsa* (**CONSOB**) pursuant to Italian laws and regulations. Accordingly, (i) neither these Listing Particulars nor any other offering material relating to the Securities may be distributed or made available in the Republic of Italy and (ii) no marketing, promotional, informative or solicitation activity whatsoever can be performed in the Republic of Italy.

## **Singapore**

These Listing Particulars have not been registered as a prospectus with the Monetary Authority of Singapore (the **MAS**). Accordingly, the Securities have not been, and will not be, offered or sold or caused to be made the subject of an invitation for subscription or purchase, nor have these Listing Particulars or any other document or material in connection with the offer or sale, or invitation for subscription or purchase, of the Securities been circulated or distributed, nor will they be circulated or distributed, whether directly or indirectly, to any person in Singapore other than: (a) to an institutional investor (as defined in Section 4A of the Securities and Futures Act (Chapter 289 of Singapore) (the **SFA**) pursuant to Section 274 of the SFA; (b) to a relevant person (as defined in Section 275(2) of the SFA) pursuant to Section 275(1) of the SFA, or any person pursuant to Section 275(1A) of the SFA, and in accordance with the conditions specified in Section 275 of the SFA; or (c) otherwise pursuant to, and in accordance with the conditions of, any other applicable provision of the SFA.

Where the Securities are subscribed or purchased under Section 275 of the SFA by a relevant person which is:

- (a) a corporation (which is not an accredited investor (as defined in Section 4A of the SFA)) the sole business of which is to hold investments and the entire share capital of which is owned by one or more individuals, each of whom is an accredited investor; or
- (b) a trust (where the trustee is not an accredited investor) whose sole purpose is to hold investments and each beneficiary of the trust is an individual who is an accredited investor,

securities (as defined in Section 239(1) of the SFA) of that corporation or the beneficiaries’ rights and interest (howsoever described) in that trust shall not be transferred within six months after that corporation or that trust has acquired the Securities pursuant to an offer made under Section 275 of the SFA except:

- (1) to an institutional investor or to a relevant person defined in Section 275(2) of the SFA, or to any person arising from an offer referred to in Section 275(1A) or Section 276(4)(i)(B) of the SFA;
- (2) where no consideration is or will be given for the transfer;

- (3) where the transfer is by operation of law;
- (4) as specified in Section 276(7) of the SFA; or
- (5) as specified in Regulation 32 of the Securities and Futures (Offers of Investments) (Shares and Debentures) Regulations 2005 of Singapore.

## **Switzerland**

The Securities may not be publicly offered in Switzerland and will not be listed on the SIX Swiss Exchange (**SIX**) or on any other stock exchange or regulated trading facility in Switzerland. These Listing Particulars do not constitute an issue prospectus under art. 652a or art. 1156 of the Swiss Code of Obligations or a listing prospectus under art. 27 ff. of the SIX Listing Rules or the listing rules of any other stock exchange or regulated trading facility in Switzerland and has been prepared without regard to the disclosure standards thereunder. Neither these Listing Particulars nor any other offering or marketing material relating to the Society or the Securities may be publicly distributed or otherwise made publicly available in Switzerland.

Neither these Listing Particulars nor any other offering or marketing material relating to the Society or the Securities have been or will be filed with or approved by any Swiss regulatory authority. In particular, this document will not be filed with, and the offer of Securities will not be supervised by, the Swiss Financial Market Supervisory Authority FINMA, and the offer of Securities has not been and will not be authorised under the Swiss Federal Act on Collective Investment Schemes (the **CISA**). The investor protection afforded to acquirers of interests in collective investment schemes under the CISA does not extend to acquirers of Securities.

## **General**

Any purchase, offer, sale or delivery of the Securities must comply with all applicable securities laws and regulations in force in any jurisdiction in which purchases, offers, sales or deliveries of the Securities take place, or where these Listing Particulars are possessed or distributed. Any consent, approval or permission required for the purchase, offer, sale or delivery of the Securities under the laws and regulations in force in any relevant jurisdiction in which such purchases, offers, sales or deliveries are made must be obtained, and the Society shall have no responsibility therefor. The Society makes no representation as to whether the Securities may at any time be lawfully sold in compliance with any applicable registration or other requirements in any jurisdiction, or pursuant to any exemption available thereunder, nor does it assume any responsibility for facilitating such sale.

## **4. SETTLEMENT**

The CCDS and Tier 2 Notes are expected to be issued on or around 12 April 2018. Admission of the CCDS and Tier 2 Notes to the Official List of the Luxembourg Stock Exchange and to trading on the Euro MTF is expected to occur on or around the date of issue of the Securities.

## **5. MINIMUM INVESTMENT AND TRANSFERS**

**CCDS:** The CCDS are subject to a minimum transfer amount, initially fixed at 500 CCDS. The minimum transfer amount will not be reduced except in agreement with the Relevant Regulators. Accordingly, the minimum initial investment in CCDS will be not less than 500 CCDS (reflecting a minimum total consideration of approximately £50,000 at the issue price of £100 per CCDS).

A purported transfer of CCDS in the secondary market will not be valid, and will not be registered in the CCDS register or accepted by the Clearing Systems, unless the number of CCDS transferred is a whole number that is equal to or greater than the minimum transfer amount prevailing at the time of transfer.

**Tier 2 Notes:** The Tier 2 Notes have denominations consisting of a minimum denomination of £1,000 and higher denominations that are integral multiples of £100 above such minimum denomination. Accordingly, the minimum initial investment in CCDS will be not less than £1,000 in principal amount.

Transfers of the Tier 2 Notes in the secondary market must be effected in principal amounts equal to £1,000 or a higher integral multiple of £100 thereabove, and purported transfers in any other amounts will not be registered in the Tier 2 Notes register or accepted by the Clearing Systems.

## 6. DETAILS RELATING TO HOW SECURITIES TO BE HELD IN CLEARING SYSTEMS

All of the CCDS will, upon issue, be represented by a single certificate (the **Global CCDS Certificate**). All of the Tier 2 Notes will, upon issue, be represented by a single certificate (the **Global Tier 2 Certificate** and, together with the Global CCDS Certificate, the **Global Certificates**).

The Global Certificates will be registered in the name of the Nominee and may be delivered on or prior to the issue date of the Securities. Upon the registration of the Global Certificates in the name of the Nominee and delivery of the Global Certificates to the Nominee, the Clearing Systems will credit each subscriber with a number of CCDS and/or a principal amount of Tier 2 Notes (as the case may be) for which it has subscribed. Transfers of book-entry interests in the Securities will be effected through the records of the Clearing Systems and their respective participants in accordance with the rules and procedures of the Clearing Systems and their respective participants.

The Nominee shall be the sole owner of legal title to all of the CCDS and Tier 2 Notes represented by the Global Certificates, and shall be the sole registered holder for all of the CCDS and Tier 2 Notes for the purposes of the Rules and the terms of the Securities.

Registration of title to CCDS and/or Tier 2 Notes in a name other than that of the Nominee will be permitted only if the Clearing Systems have closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or do in fact do so and no successor or alternative clearing system is available. Accordingly, the Society would not expect any CCDS or Tier 2 Notes to be held directly by any person other than the Nominee (or any successor or replacement nominee), and expects that investors in the CCDS and the Tier 2 Notes will therefore continue to hold beneficial interests in those Securities through the Clearing Systems (and any relevant intermediaries).

A holder of any beneficial interests in respect of CCDS in the Clearing Systems will not become a member of the Society by virtue of its investment in the CCDS and will only indirectly benefit from the CCDS Conditions, the Rules, the Memorandum or the Act with respect to the CCDS through the Nominee. The holding structure for CCDS has a number of consequences for investors, including with respect to member voting rights and rights to conversion benefits in the event of a demutualisation of the Society as described in “*Part I: Risk Factors*” under “*Investors in the CCDS will hold beneficial interests in the CCDS through an account with a Clearing System, will not be members of the Society by virtue of their investment in CCDS and must rely on the relevant Clearing System’s procedures*”, “*Investors will have no voting rights at general meetings of the members of the Society for so long as the CCDS are held through an account with a Clearing System*” and “*For so long as the CCDS are held in an account with a Clearing System, the Holders thereof will not be entitled to Conversion Benefits arising on a demutualisation or other transfer of the Society’s business to a company*”.

The Tier 2 Notes, in contrast to the CCDS, are a subordinated debt of the Society and holders of Tier 2 Notes are creditors of the Society, not members. As such, ownership of the Tier 2 Notes would not confer any member voting rights on holders, regardless of how the Tier 2 Notes are held.



Investors holding their Securities through the Clearing Systems, shall be entitled to rights in respect of its beneficial interest in the CCDS as prescribed by the rules of the relevant Clearing System and must rely on the procedures of such relevant clearing systems to enforce its rights.

For so long as the Securities are represented by the Global Certificates, the Society's payment obligations in respect of the Securities will be discharged upon payment by or on behalf of the Society to, or to the order of, the Nominee. Holders of beneficial interests in the Clearing Systems must look to the Clearing Systems (or the intermediary through which they hold their beneficial interests) for their share of any such payment made to the Clearing Systems.

## **PART VIII - OVERVIEW OF CERTAIN PROVISIONS OF THE RULES OF THE SOCIETY AND THE ACT RELATING TO THE CORE CAPITAL DEFERRED SHARES**

The rights and restrictions attaching to the Core Capital Deferred Shares will be governed by the rules of the Society (the **Rules**), certain provisions of the Building Societies Act 1986, as amended (the **Act**) and the Conditions of Issue of the Core Capital Deferred Shares (the **CCDS Conditions**). Set out below is an overview of the key provisions of the Rules and certain provisions of the Act insofar as they might affect the rights of the CCDS holders, together with certain explanatory notes which are italicised. Terms defined in the Rules or the CCDS Conditions will, unless otherwise defined herein or the context otherwise requires, have the same meanings when used in this overview.

The Tier 2 Notes are, by contrast, a subordinated debt of the Society and, as such, holders of the Tier 2 Notes are creditors of the Society rather than members. The rights and restrictions attaching to the Tier 2 Notes are governed by the Terms and Conditions of the Tier 2 Notes (the **Tier 2 Conditions**) as set out as “*Part X: Terms and Conditions of the Tier 2 Notes*”.

### **1. GENERAL**

A person who holds a Share with the Society (including a CCDS) is a Shareholding Member of the Society. The CCDS are Core Capital Deferred Shares for the purposes of the Rules and therefore a person whose name is entered in the CCDS Register (as defined below) as a CCDS holder is a Shareholding Member of the Society.

Each CCDS holder, and all persons claiming through it or on its behalf or under the Rules, shall be bound by the Rules, by the Memorandum of the Society and by the Act.

*The CCDS will be held by investors through accounts with a Clearing System and will be registered in the name of the Nominee who shall be the CCDS holder for the purposes of the Rules and the CCDS Conditions. An investor holding beneficial interests in the CCDS through a Clearing System will not be a member of the Society by virtue of its investment in the CCDS and (without prejudice to any rights or obligations that such person may have as a member of the Society in some other capacity) will be only indirectly subject to the Rules, the Memorandum and the Act with respect to its holding of CCDS in the manner provided above. Investors holding beneficial interests in the CCDS through a Clearing System shall be entitled to the rights in respect of their beneficial interests as prescribed by the rules of that Clearing System.*

*Registration of title to CCDS in a name other than that of the Nominee will be permitted only if all the Clearing Systems have closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or announce an intention permanently to cease business or do in fact do so. The Society considers this to be unlikely to occur. For so long as the CCDS remain held in accounts with a Clearing System, references in this Part to “CCDS holders” and related expressions shall be read as references to the Nominee.*

### **2. REGISTER**

The Society shall maintain records constituting the register of members for the purposes of the CCDS (the **CCDS Register**) which shall be a separate Deferred Shares Register for the purposes of the Rules, in which shall be entered the name and address of each CCDS holder. Each CCDS holder shall notify the Society immediately of any change of name or address and shall produce such evidence of such change as the Society may require.

Transfers and other documents or instructions relating to or affecting the title to any CCDS shall also be recorded in the CCDS Register. No charge shall be made in respect of any entry in the CCDS

Register. The CCDS Register shall be maintained at the Principal Office, or at such other place as the board of directors of the Society thinks fit.

The Society has appointed Citibank N.A., London Branch at *6th floor, Citigroup Centre, Canary Wharf, London E14 5LB, United Kingdom* as its registrar for the CCDS.

### 3. DISTRIBUTIONS

#### *Cap on Distributions*

The CCDS are a Core Capital Deferred Shares for the purposes of the Rules. The Rules provide that any Core Capital Deferred Shares must be issued on terms that limit the amount of the Periodic Distributions (**Distributions**) that may be paid on such investment in respect of any given financial year to not more than the applicable Periodic Distributions Cap (the **Cap**), in order to protect the reserves of the Society.

The Rules provide that the initial Cap, which would have been applicable to Distributions in respect of the financial year to 31 March 2015 had CCDS been in issue during that financial year, was £15 per CCDS, and that (subject as stated below) in respect of each subsequent financial year the Cap will be adjusted for inflation by reference to the United Kingdom Consumer Price Index (overall index, 2005=100) (**CPI**) published by the Office for National Statistics (or any successor to that index). Such adjustment will be made by applying the CPI annual inflation percentage published by the Office for National Statistics in its statistical bulletin for the last full calendar month of the financial year in respect of which the Distributions are payable (being the percentage increase or decrease over the twelve months to and including that month) to the prevailing Cap.

The prevailing Cap in respect of the financial year to 31 March 2017 was £15.42. For illustrative purposes only (as the Board is not intending to declare any Distributions in respect of the Society's financial year to 31 March 2018), the Cap on Distributions for the financial year to 31 March 2018 will be determined by applying the CPI annual inflation percentage published by the Office for National Statistics in its statistical bulletin for March 2018 to the prevailing Cap in respect of the financial year to 31 March 2017 of £15.42.

If the CPI ceases to be published and no direct successor or replacement index is published, the Board shall be entitled to determine an appropriate replacement index for determining future inflation-based adjustments to the Cap, and shall have sole discretion to determine any modifications to the method of determining inflation-based adjustments to the Cap during the transition from CPI to the replacement index. The Society shall in each year determine the adjustment to the Cap promptly following publication of the relevant CPI (or successor or replacement index) data by the Office for National Statistics (or such successor or other organisation as may be responsible for publishing official data with respect to the relevant index) and will notify the members of the Society of the adjusted Cap not later than at the first Annual General Meeting following publication of the relevant data.

In the event that adjustment of the Cap in the manner described above would prejudice the regulatory capital treatment of the CCDS, the Society will disapply those adjustment provisions and the Cap will revert to £15 per CCDS.

#### *Distribution Policy*

The Rules also provide that the Board may determine and from time to time publish the policy of the Society in relation to the Distributions on any Core Capital Deferred Shares and shall have regard to the ongoing profitability and long-term viability of the Society, the need for the Society to ensure that it has adequate capital resources and such other factors as the Board considers appropriate.

With respect to the Distribution Policy of the Board as at the date of these Listing Particulars, see paragraph 3 “*Distribution Policy in respect of the CCDS*” of “*Part V: – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy*” above.

#### **4. MEETINGS OF THE MEMBERS OF THE SOCIETY**

As a Shareholding Member of the Society, each CCDS holder will, subject to the provisions of the Rules, enjoy various membership rights. In particular, CCDS holders will, subject to the Rules, be entitled to receive notice of, to participate in a requisition for, to propose resolutions at, to attend, to be counted in a quorum at and to vote at any general meeting or in a Ballot of the Society.

Each CCDS holder entered in the CCDS Register will be entitled to exercise one vote (irrespective of the number of CCDS held by it or the size or number of other relevant investments or interests (if any) conferring membership rights which it may have in the Society) on a resolution at any general meeting or in a Ballot (whether an Ordinary Resolution or Special Resolution or (subject to the Rules) a Shareholding Members’ Resolution, but not a Borrowing Members’ Resolution) if that CCDS holder held the CCDS:

- (a) at the end of the financial year before the voting date; or
- (b) if the voting date falls during that part of the financial year which follows the conclusion of the Annual General Meeting commenced in that year, at the beginning of 56 days immediately preceding the voting date for Members voting in person at a special general meeting or a Ballot,  
  
as the case may be; and
- (c) on the voting date; and
- (d) the CCDS holder has not ceased to hold Shares at any time between the time referred to in (a) or (b) above (as applicable) and the voting date.

*The members’ rights attaching to the CCDS held through the Clearing Systems will be held by the Nominee. Such Nominee will be entered in the CCDS Register as the holder of CCDS held in this manner, and will be entitled to exercise the voting and other members’ rights attributable to all those CCDS so held. Accordingly, the Nominee shall have one vote (regardless of the number of CCDS held by it and regardless also of the size and number of other relevant investments or interests (if any) conferring membership rights which the Nominee may have in the Society) on a resolution at any general meeting of the Society or in a Ballot.*

*Given the difficulty of casting the single vote in a manner which reflects the views of all investors holding CCDS through the Clearing Systems and the relative insignificance of that vote in the context of all the votes which may be cast by members of the Society, the Nominee has informed the Society that it does not intend to exercise its vote insofar as such vote relates to its holding of CCDS.*

*The foregoing provisions relate to general meetings of the members of the Society. For provisions relating to the convening of separate meetings of the CCDS holders only, see CCDS Condition 12 and “Meetings; membership rights whilst the CCDS are held through Clearing Systems” under “Overview of Provisions Relating to the CCDS While Represented by the Global CCDS Certificate” in “Part IX: Conditions of Issue of the Core Capital Deferred Shares”.*

#### **5. WINDING-UP OR DISSOLUTION**

The Rules provide that upon the winding-up of the Society, or upon it being dissolved by consent, any surplus remaining after payment in full of the Society’s creditors and repayment to Members of the

amount of their Shares (together with interest due thereon) according to their priority under their respective terms and conditions of issue (but excluding Core Capital Deferred Shares unless and to the extent provided in their terms and conditions of issue), shall be divided among:

- (i) qualifying Members in proportion to the value of their Shareholding (excluding any Deferred Shares) at the relevant date;
- (ii) up to 20% to holders of Deferred Shares (excluding Core Capital Deferred Shares) at the relevant date subject to, and in proportion to the amount specified in, or calculated by reference to, their terms and conditions of issue; and
- (iii) holders of Core Capital Deferred Shares at the relevant date subject to, and in proportion to the amount specified in, or calculated by reference to, their terms and conditions of issue.

The relevant date is the earlier of either the date of notice of a winding-up or dissolution resolution or the date of presentation of a winding-up petition or such other date as may be specified by the insolvency official appointed with primary responsibility for the winding-up or dissolution of the Society.

If there are insufficient assets to repay all Members the amounts payable on their Shares in accordance with their terms and conditions of issue, no repayments shall be made in respect of any Deferred Share until after all other Members have been repaid in full.

For these purposes, **qualifying Members** means Persons who hold on the relevant date, and have held, throughout the period of two years up to that date, Shares (excluding any holding of Deferred Shares) to the value of not less than £100.

*On a winding-up or dissolution of the Society, the rights of the CCDS holders to participate in the winding-up or dissolution will, subject as provided in CCDS Condition 4.8, be limited to an entitlement to share, to the extent and in the manner provided in the CCDS Conditions, in the Surplus (if any) of the Society remaining following payment of all amounts in respect of Liabilities of the Society and any amounts payable pursuant to CCDS Condition 4.8. If there are insufficient assets of the Society to pay all amounts in respect of Liabilities of the Society, no payment shall be made to the CCDS holders in the winding-up or dissolution of the Society.*

The liability of a CCDS holder to contribute to the winding-up or dissolution of the Society is limited to the amount which has been actually paid, or the amount (if any) which is in arrear, on such holder's CCDS. For these purposes, amounts would only be in arrear on CCDS if, and to the extent that, the Nominal Amount and Premium Amount (each as defined in the CCDS Conditions) payable in respect of such CCDS on issue had not been paid in full. As the CCDS will be paid up in full upon issue, there will be no liability of holders of CCDS to further contribute in the winding-up or dissolution of the Society.

## **6. DISPUTES AND LEGAL PROCEEDINGS**

Section 85 of, and Schedule 14 to, the Act provide that no court other than the High Court of Justice in England shall have jurisdiction to hear and determine disputes between a building society and a member or a representative of a member in that capacity in respect of any rights or obligations arising from the rules of a building society or the Act. Under various other enactments, the High Court is empowered to transfer cases over which it has jurisdiction to the County Court.

## PART IX – CONDITIONS OF ISSUE OF THE CORE CAPITAL DEFERRED SHARES

*The following (save for paragraphs in italics, which do not form part of the conditions) are the conditions of issue of the CCDS as they apply to holders of the CCDS and in the form in which they will appear on the reverse of each CCDS Certificate:*

The Core Capital Deferred Shares (the **CCDS**, which term shall include any further core capital deferred shares issued pursuant to Condition 13 which are consolidated and form a single series with the CCDS) are issued under the Rules (the **Rules**) of West Bromwich Building Society (the **Society**) for the time being. CCDS holders are entitled to the benefit of, are bound by and are deemed to have notice of, the Rules. The CCDS are also issued subject to, and with the benefit of, these conditions of issue (the **Conditions**) and subject to an agency agreement (as amended from time to time, the **Agency Agreement**) dated on or around 12 April 2018 between the Society and Citibank N.A., London Branch as registrar and transfer agent (in such capacities, the **Registrar**, which term shall include any other registrar and transfer agent appointed by the Society in respect of the CCDS from time to time) and principal paying agent (in such capacity, the **Principal Paying Agent**, which term shall include any other principal paying agent appointed by the Society in respect of the CCDS from time to time). In the event of inconsistency between the Rules, these Conditions and the Agency Agreement, the Rules will prevail and, subject thereto, in the event of inconsistency between these Conditions and the Agency Agreement, these Conditions will prevail. CCDS holders are bound by and are deemed to have notice of all the provisions of the Agency Agreement applicable to them.

*The CCDS will be held through accounts with the Clearing Systems and will only be issued in definitive form in the very limited circumstances described under “Overview of Provisions Relating to the CCDS While Represented by the Global CCDS Certificate – Exchange of the Global CCDS Certificate and Registration of Title”. While CCDS are held on behalf of investors through an account with a Clearing System, CCDS will be registered in the name of the Nominee. The Nominee shall be the CCDS holder for all of the CCDS for the purposes of the Conditions, and not the investors holding beneficial interests in the CCDS through the Clearing Systems. The investors holding the beneficial interests in CCDS through Clearing System accounts shall be entitled to the rights in respect of their beneficial interests as prescribed by the rules of the relevant Clearing System.*

### 1. GENERAL

- 1.1 Terms defined in the Rules will, unless otherwise defined herein or unless the context otherwise requires, have the same meanings when used in these Conditions. Other capitalised terms used in these Conditions shall have the meanings set out in Condition 17.
- 1.2 The CCDS:
  - (a) are deferred shares for the purposes of section 119 of the Building Societies Act 1986, as amended (the **Act**);
  - (b) are not protected deposits for the purpose of the Financial Services Compensation Scheme established under the Financial Services and Markets Act 2000 as amended (the **FSMA**);
  - (c) are not withdrawable; and
  - (d) are Core Capital Deferred Shares for the purposes of the Rules.
- 1.3 By purchasing CCDS, each CCDS holder agrees to assign any rights to Conversion Benefits to which it may become entitled by reason of its holding of CCDS to a charity nominated by the Society pursuant to any scheme for charitable assignment established by the Society for the time being. For these purposes, **Conversion Benefits** shall mean any benefits under the terms of any future transfer of the Society’s business to a company (other than rights to receive ordinary shares issued by the Successor

Entity or its parent, as specifically provided for under Condition 10) and, if the Society merges with any other building society, the Society shall, after the date of such merger, extend to such other society.

- 1.4 If a CCDS holder fails to assign any Conversion Benefits as required pursuant to Condition 1.3, it acknowledges that, by purchasing CCDS, it waives its entitlement to retain any Conversion Benefits received by it and covenants promptly to pay and deliver such Conversion Benefits to a selected charity nominated by the Society pursuant to any scheme for charitable assignment established by the Society (or to the Society for payment and delivery to the selected charity) and until such time as payment is made, will hold a sum equal to such amount on trust for the selected charity.

*As investors holding the beneficial interests in CCDS through Clearing System accounts will not, by virtue of such holding, be Members of the Society they will not be entitled to any Conversion Benefits by virtue of such holding. Any Conversion Benefits relating to the CCDS will belong instead to the Nominee, as the registered holder of the CCDS in the CCDS Register. The Nominee will, on or prior to date of issue of the CCDS, irrevocably agree to assign to a selected charity nominated by the Society pursuant to any scheme for charitable assignment established by the Society any Conversion Benefits.*

## **2. FORM, TITLE AND TRANSFER**

### **2.1 Form**

The CCDS are in registered form and have a nominal value of £1 each (the **Nominal Amount**). The CCDS are transferable in accordance with the Rules and subject to Condition 2.2.

In the event that a CCDS is subscribed at a price higher than the Nominal Amount, the difference between the subscription price and the Nominal Amount shall constitute CCDS premium (the **Premium Amount**).

### **2.2 Title and transfer**

Title to the CCDS passes only by registration in the CCDS Register. The holder of any CCDS will (except as otherwise required by law) be treated as its absolute owner for all purposes (regardless of any notice of ownership, trust or any other interest or any writing on, or the theft or loss of, the CCDS Certificate issued in respect of it) and no person will be liable for so treating the holder.

CCDS are transferable in whole numbers and no CCDS may be transferred in part. A transfer of CCDS will not be valid, and will not be registered in the CCDS Register, unless the number of CCDS transferred is equal to or greater than the specified minimum transfer amount (the **Minimum Transfer Amount**) prevailing at the time of transfer. The initial Minimum Transfer Amount is 500 CCDS. The Minimum Transfer Amount may be reduced in agreement with the Relevant Regulators upon not less than 30 nor more than 60 days' notice to CCDS holders in accordance with Condition 14. The Minimum Transfer Amount prevailing from time to time will be published on the Society's website.

No legal transfer of a CCDS shall be valid unless made in the form endorsed on the CCDS Certificate or in such other form as the Board may agree, which form shall be duly completed and signed (as appropriate) and presented to the Registrar. Legal title to the CCDS will pass upon registration of such transfer in the CCDS Register and, if so requested in writing by the registered holder, the Registrar shall, on behalf of the Society, issue a CCDS Certificate in respect of such holding (which will be made available at the specified office of the Registrar).

*It will not be possible for investors to transfer CCDS in amounts less than the Minimum Transfer Amount prevailing as at the time of transfer. The Clearing Systems will not accept instructions to settle transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount, and (in the limited circumstances in which definitive CCDS are issued) the Registrar will not register in the CCDS Register any transfer of CCDS in definitive form in amounts less than the prevailing Minimum Transfer*

*Amount. Accordingly, purported transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount will be incapable of settlement. Investors in CCDS are responsible for ensuring that any trades they enter into in respect of the CCDS are capable of settlement; failure to do so may result in an investor breaching its contract of sale and purchase.*

*Any decision by the Society to propose a reduction in the Minimum Transfer Amount to the Relevant Regulators will be based on all relevant factors at the time, which may include (if it is the case) the fact that an established trading market has developed for the CCDS which would enable a wider range of investors to better assess whether or not CCDS would be a suitable investment for them. The Society does not expect to make any such proposal in the near term or to make such proposals frequently.*

## **2.3 CCDS Certificates**

A certificate (each a **CCDS Certificate**) will, if so requested in writing by such CCDS holder, be issued to each CCDS holder in respect of its registered holding of CCDS. Each CCDS Certificate will be numbered serially with an identifying number which will be recorded on the relevant CCDS Certificate and in the CCDS Register, and will specify the number of CCDS registered in the name of such holder(s).

Each new CCDS Certificate to be issued following a transfer will be mailed by uninsured mail at the risk of the holder entitled to the CCDS to the address specified in the form of transfer within one month of the date of registration of the transfer in the CCDS Register (or, if later, within one month of the written request of the relevant CCDS holder to be issued a CCDS Certificate).

Where some but not all of the CCDS in respect of which a CCDS Certificate is issued are to be transferred, a new CCDS Certificate in respect of the number of CCDS not so transferred will, within 14 days of receipt by the Registrar of the original CCDS Certificate, be mailed by uninsured mail at the risk of the holder of the CCDS not so transferred to the address of such holder appearing on the CCDS Register or as specified in the form of transfer.

*Except in the limited circumstances described under “Overview of Provisions Relating to the CCDS While Represented by the Global CCDS Certificate — Exchange of the Global CCDS Certificate and Registration of Title”, owners of interests in the CCDS will not be entitled to receive physical delivery of CCDS Certificates.*

## **2.4 Formalities free of charge**

Registration of transfer of CCDS will be effected without charge by or on behalf of the Society or the Registrar but upon payment (or the giving of such indemnity as the Society or the Registrar may reasonably require) in respect of any tax or other governmental charges which may be imposed in relation to such transfer.

## **3. CCDS REGISTER**

**3.1** The Society has appointed the Registrar to act as registrar and transfer agent in respect of the CCDS under the terms of the Agency Agreement.

**3.2** Pursuant to the Agency Agreement, the Society shall procure that the Registrar maintains the CCDS Register (which shall be a separate Deferred Shares Register for the purposes of the Rules), in which shall be entered the name and address of each CCDS holder. Each CCDS holder shall notify the Registrar immediately of any change of name or address and shall produce such evidence of change of name or address as the Registrar may reasonably require.



**3.3** A CCDS holder must provide the Registrar with a written order containing such instructions and other information as the Society and the Registrar may reasonably require to complete, execute and deliver a CCDS Certificate to such CCDS holder.

**3.4** Transfers and other documents or instructions relating to or affecting the title of any CCDS shall be recorded in the CCDS Register. No charge shall be made in respect of any entry in the CCDS Register or any change in relation to such entry. The CCDS Register shall be maintained at the specified office of the Registrar or at such other place as the Society and the Registrar shall agree.

#### **4. STATUS, SUBORDINATION AND RIGHTS ON A WINDING-UP**

##### **4.1 Status and subordination**

The CCDS constitute direct, unsecured and subordinated investments in the Society and, on a winding-up or dissolution of the Society, rank (a) *pari passu* among themselves and with any other investments ranking or expressed to rank *pari passu* with the CCDS (provided that participation of CCDS holders in the Surplus (as defined in Condition 4.2) will be in the manner and proportion described in this Condition 4), and (b) junior to (i) all Liabilities of the Society and (ii) any claims in respect of declared, unconditional and unpaid Distributions in accordance with Condition 4.8 and claims ranking or expressed to rank *pari passu* therewith.

##### **4.2 Rights on a winding-up or dissolution**

On a winding-up or dissolution of the Society, the rights of the holders of Outstanding CCDS to participate in the winding-up or dissolution shall, save as provided in Condition 4.8, be limited to an entitlement to share, to the extent and in the manner provided in Condition 4.3, in the surplus assets (if any) of the Society remaining (**Surplus**) following payment of all amounts in respect of Liabilities of the Society and any amounts payable pursuant to Condition 4.8 and claims ranking or expressed to rank *pari passu* therewith, provided that such entitlement shall be capped at the Average Principal Amount per CCDS as provided in Condition 4.7.

##### **4.3 Distribution of Surplus**

In the event of a distribution of Surplus, such Surplus shall, subject to Condition 4.7, be shared without preference as to priority between:

- (a) CCDS holders (whose entitlement shall be for such amount as will, upon such sharing of the Surplus, result in CCDS holders receiving, in respect of each CCDS held which is Outstanding at the Relevant Time, an amount equal to (i) the Core Capital Contribution Share determined in accordance with Condition 4.4 or, if less (ii) the Average Principal Amount determined as at the Relevant Time in accordance with Condition 4.5);
- (b) qualifying Members (whose entitlement shall be calculated based on the amount of their Shareholding (excluding any Deferred Shares) at the Relevant Time) (where **qualifying Member**, **Shareholding** and **Deferred Share** have their respective meanings given in the Rules);
- (c) (unless the terms of the relevant deferred shares otherwise provide and subject to any limit specified in the Rules from time to time) holders of any other Deferred Shares at the Relevant Time (whose entitlement (if any) shall be calculated based on and subject to the terms of issue of such Deferred Shares); and
- (d) any other persons entitled to share in the surplus assets in accordance with the Rules from time to time (whose entitlement shall be calculated based on and subject to the Rules).

In these Conditions, **Relevant Time** means (i) the time at which an instrument or order is made (including, without limitation, an order made under a building society insolvency or building society special administration (each as defined in the Act)) or an effective resolution is passed for the winding-up or (otherwise than by virtue of section 93(5) (dissolution following an amalgamation with one or more building societies by the establishment of a successor building society), section 94(10) (dissolution following transfer of all engagements to another building society) or section 97(9) or (10) (dissolution following transfer of the whole business to a company) of the Act) dissolution of the Society, or (ii) such other time as may be specified by the administrator, receiver, liquidator or other insolvency official appointed with primary responsibility for the winding-up or dissolution of the Society.

#### 4.4 Core Capital Contribution Share

*This Condition 4.4 determines the amount of any Surplus the CCDS holders will be eligible to receive upon a winding-up of the Society (unless the amount calculated in accordance with this Condition 4.4 exceeds the Average Principal Amount per CCDS calculated in accordance with Condition 4.5, in which case CCDS holders will instead be eligible to receive the Average Principal Amount for each CCDS held). For the avoidance of doubt, if the Society is wound up and there is no Surplus, CCDS holders will not be eligible to receive any amount pursuant to this Condition 4.4 or Condition 4.5.*

*The calculation in Condition 4.4(b) determines the relative contribution proportion (expressed as a percentage) of the CCDS holders (as a class) to the total Common Equity Tier 1 Capital of the Society from time to time. This Core Capital Contribution Proportion will be adjusted upon recalculation from time to time to reflect any additional issues of CCDS pursuant to Condition 13 and any cancellations of CCDS. If the Society is wound up in circumstances where a Surplus is available for distribution, Condition 4.4(a) provides that the CCDS holders (as a class) would be eligible to receive such share (i.e. percentage) of that Surplus as is equal to the Core Capital Contribution Proportion prevailing at that time, which amount would be shared amongst the CCDS holders pro rata based on the number of CCDS they hold.*

*In addition to recognising new issues and cancellations of CCDS from time to time, the calculation in Condition 4.4(b) also recognises that the CCDS holders have a notional proportionate interest in the profits and losses of the Society on an ongoing basis: each time the calculation is repeated, the section of the formula “ $(CCCP_{DT-1} \times \text{Core Capital}_{DT})$ ” effectively apportions to outstanding CCDS a notional interest in the appropriate proportion of profits generated or losses incurred (recognised as increases or decreases in Common Equity Tier 1 Capital) in the period between the previous calculation and the current calculation. The amount of those profits or losses attributed to the CCDS is based on the Core Capital Contribution Proportion prevailing at the time those profits were generated or losses incurred. Thus all CCDS will have a notional proportionate interest in the profits and losses of the Society from their time of issue (subject, on a winding-up or dissolution, to Condition 4.5). For the avoidance of doubt, the calculation is relevant for determining the proportion of any Surplus that CCDS holders would be eligible to receive upon the winding-up or dissolution of the Society. The notional proportionate interest in profits is not an entitlement to receive any amounts in respect of such profits at any time. Except for any payment of Surplus upon the winding-up or dissolution of the Society, no payments will be made to CCDS holders as a result of the calculation being performed.*

- (a) The **Core Capital Contribution Share** means the amount (rounded to the nearest penny, with £0.005 being rounded up) calculated by (i) multiplying (x) the total amount of Surplus available for distribution in accordance with Condition 4.2 by (y) the Core Capital Contribution Proportion calculated in accordance with Condition 4.4(b) as at the Relevant Time and (ii) dividing the resulting figure by the total number of CCDS which are Outstanding as at the Relevant Time.
- (b) The **Core Capital Contribution Proportion** at any given Determination Time (as defined below) is the portion (expressed as a percentage) of the total Common Equity Tier 1 Capital of

the Society at such time which is determined, in accordance with the following provisions of this Condition 4.4(b), to have been contributed by the CCDS which are Outstanding at such time.

- (i) The Core Capital Contribution Proportion shall be calculated as at the time of issue of the first tranche of CCDS and recalculated (A) as at the time of each issue of Additional CCDS (as defined in Condition 13), (B) upon the cancellation of any CCDS and (C) as at the Relevant Time (the time of each such calculation, a **Determination Time**). For the purposes of calculating the Core Capital Contribution Proportion at the Relevant Time (but not at any other Determination Time), all CCDS held by the Society in its treasury function at the Relevant Time shall be deemed to be cancelled at the Relevant Time (such cancellation to be reflected in the determination of the Core Capital Contribution Proportion at the Relevant Time).
- (ii) The Core Capital Contribution Proportion as at each Determination Time shall be determined by the Board (or, if applicable, in the case of determination as at the Relevant Time, by or on behalf of the administrator, receiver, liquidator or other insolvency official appointed with primary responsibility for the winding-up or dissolution of the Society) on the basis of the most recently published consolidated annual, interim or *ad hoc* accounts of the Society available as at the relevant Determination Time, and such determination shall be reviewed and confirmed by an independent accountant or firm of accountants of recognised standing appointed or approved by the Board (or, if applicable, the relevant insolvency official) as an expert for such purpose (provided that such expert shall have no responsibility or liability whatsoever to CCDS holders in connection with such review and confirmation).
- (iii) The Core Capital Contribution Proportion for a particular Determination Time (**DT**) shall be a percentage (rounded to five decimal places, with 0.000005 being rounded up) equal to:

$$\frac{\text{New Issue Amount}_{DT} + (\text{CCCP}_{DT-1} \times \text{Core Capital}_{DT}) - \text{Cancellation Adjustment Share}_{DT}}{\text{New Issue Amount}_{DT} + \text{Core Capital}_{DT} - \text{Cancellation Adjustment Amount}_{DT}}$$

where:

**New Issue Amount<sub>DT</sub>** is the sum of the aggregate Nominal Amounts and aggregate Premium Amounts (in each case expressed in pounds sterling) of the CCDS (if any) being issued at time DT (and shall be zero if no CCDS are being issued at time DT);

**CCCP<sub>DT-1</sub>** is the Core Capital Contribution Proportion calculated as at, and applicable to, the Determination Time immediately preceding time DT (**DT-1**) (provided that, for the purposes of determining the Core Capital Contribution Proportion at the first Determination Time upon issue of the first tranche of CCDS, CCCP<sub>DT-1</sub> shall be zero);

**Core Capital<sub>DT</sub>** is the total amount of Common Equity Tier 1 Capital of the Society, calculated in accordance with the Capital Rules, as at time DT, adjusted if necessary to disregard the impact of (i) any New Issue Amount<sub>DT</sub> as a result of any new CCDS being issued at time DT, (ii) any Cancellation Adjustment Amount<sub>DT</sub> as a result of any CCDS being cancelled at time DT and (iii) any CCDS held, as a result of treasury trading, by the Society in its treasury function as at time DT, in each case having regard to the Capital Rules and accounting standards then applicable;

**Cancellation Adjustment Amount<sub>DT</sub>** is the amount (expressed in pounds sterling) by which the Common Equity Tier 1 Capital of the Society is or was reduced as a

result of the purchase by the Society of the CCDS (if any) which are being cancelled at time DT (and shall be zero if no CCDS are being cancelled at time DT); and

**Cancellation Adjustment Share<sub>DT</sub>** is an amount (which, for the avoidance of doubt, shall be zero if no CCDS are being cancelled at time DT) equal to:

$$(N \times \text{Notional}_{DT}) + \text{CCCP}_{DT-1}[\text{Cancellation Adjustment Amount}_{DT} - (N \times \text{Notional}_{DT})]$$

where:

**N** is the number of CCDS which are being cancelled at time DT;

**Notional<sub>DT</sub>** is the deemed notional contribution (expressed in pounds sterling) of each CCDS to the Common Equity Tier 1 Capital of the Society as at the relevant Determination Time, which shall be calculated by (i) multiplying (x) Core Capital<sub>DT</sub> by (y) CCCP<sub>DT-1</sub> and (ii) dividing the resulting figure by the total number of CCDS which are Outstanding immediately prior to the relevant Determination Time; and

**Core Capital<sub>DT</sub>**, **CCCP<sub>DT-1</sub>** and **Cancellation Adjustment Amount<sub>DT</sub>** have the meanings given above.

*The “Cancellation Adjustment Share<sub>DT</sub>” formula allocates (notionally, and for the purposes only of determining the Core Capital Contribution Proportion from time to time) between CCDS holders and the other members of the Society the reduction in the Common Equity Tier 1 Capital of the Society as a result of the purchase by the Society of the CCDS which are being cancelled at the relevant Determination Time. “Notional<sub>DT</sub>” represents the deemed notional contribution of each CCDS being cancelled to the Common Equity Tier 1 Capital of the Society as at the relevant Determination Time, and such amount will (notionally, in the context of the determination of the Core Capital Contribution Proportion) be borne by the CCDS holders. If the amount of the reduction in Common Equity Tier 1 Capital per cancelled CCDS is higher or lower than such deemed notional contribution, the difference is apportioned between the CCDS holders and the other members of the Society proportionately by reference to the prevailing Core Capital Contribution Proportion.*

- (c) The Core Capital Contribution Proportion shall be determined as soon as reasonably practicable following each Determination Time and shall promptly, and in any event within 14 days following the confirmation of such determination in the manner provided in Condition 4.4(b)(ii) above, be published on the Society’s website (or, if this is not possible, via the Luxembourg Stock Exchange website ([www.bourse.lu](http://www.bourse.lu)) or a regulatory information service as may be recognised by any stock exchange on which the CCDS are for the time being listed).
- (d) If, at any time, by reason of any change in the Capital Rules (or official interpretation thereof) or otherwise, the CCDS cease to qualify as Common Equity Tier 1 Capital of the Society, they will, nevertheless, be treated as contributing to Common Equity Tier 1 Capital of the Society (on the same basis as immediately prior to ceasing so to qualify) for the purposes of determining the Core Capital Contribution Proportion.

#### 4.5 Average Principal Amount

- (a) **Average Principal Amount** means an amount (expressed in pounds sterling) per CCDS calculated as follows and rounded to the nearest penny (with £0.005 being rounded up):

$$\frac{\text{Aggregate Nominal} + \text{Aggregate Premium}}{\text{Total CCDS Issued}}$$

where:

**Aggregate Nominal** is the aggregate of all Nominal Amounts (expressed in pounds sterling) paid at initial subscription of all CCDS issued at any time up to (and including) the time at which the Average Principal Amount is being calculated (whether or not the same remain Outstanding);

**Aggregate Premium** is the aggregate of all Premium Amounts (expressed in pounds sterling) paid at initial subscription of all CCDS issued at any time up to (and including) the time at which the Average Principal Amount is being calculated (whether or not the same remain Outstanding); and

**Total CCDS Issued** is the total number of CCDS issued at any time up to (and including) the time at which the Average Principal Amount is being calculated (whether or not the same remain Outstanding).

- (b) The Average Principal Amount will be determined in accordance with this Condition 4.5 by the Board as at the time of each new issue of CCDS, and in each case shall be published on the Society's website (or, if this is not possible, via the Luxembourg Stock Exchange website ([www.bourse.lu](http://www.bourse.lu)) or a regulatory information service as may be recognised by any stock exchange on which the CCDS are for the time being listed) promptly, and in any event within 14 days, following its determination.

#### **4.6 CCDS issued other than for cash**

If at any time CCDS are issued and allotted other than for cash (including, without limitation, CCDS issued and allotted by way of a bonus issue (including a capitalisation issue) or pursuant to a remuneration scheme for directors or employees of the Society, or CCDS issued in exchange for other securities of the Society), the Premium Amount of each such CCDS shall be determined by the Board in good faith (and in accordance with generally accepted accounting practices and the accounting policies of the Society for the time being) as an amount equal to the notional value (such notional value being, as close as practicable, the equivalent cash value) in respect of which such CCDS is issued and allotted less the £1 Nominal Amount of such CCDS. The Nominal Amount and Premium Amount of each such CCDS shall be included in any calculation of the Core Capital Contribution Proportion and Average Principal Amount as if such Nominal Amount and Premium Amount had been paid to the Society in cash.

#### **4.7 Entitlement to Surplus capped**

The entitlement of CCDS holders to share in the Surplus shall be capped at the Average Principal Amount per CCDS. Accordingly, following payment to the holders of CCDS, by way of distribution of Surplus, of an amount equal to the Average Principal Amount in respect of each CCDS, the holders of the CCDS shall have no further entitlement to share in any remaining or further distribution of Surplus, and any such remaining or further Surplus shall be distributed amongst the persons and in the manner specified in Conditions 4.3(b), (c) and (d) only, or otherwise as provided in the Rules.

#### **4.8 Declared and unpaid Distributions**

On a winding-up or dissolution of the Society, the CCDS holders shall, in respect of any declared, unconditional (which term shall, for these purposes, include any conditional Distribution (as described in Condition 5.3) or part thereof in respect of which the relevant conditions have been satisfied) and unpaid Distributions, be entitled to prove in the winding-up or dissolution of the Society, as the case may be, for the amount of such Distributions but only if, and subject to the condition that, all sums due from the Society in respect of Liabilities in the winding-up or dissolution have been paid in full, and accordingly the claims of the CCDS holders in respect thereof shall rank (a) *pari passu* amongst

themselves and with any other claims ranking or expressed to rank *pari passu* therewith and (b) junior to all Liabilities of the Society. Accordingly, such claims shall constitute the most junior claim in the winding-up or dissolution of the Society other than a claim to participate in any Surplus.

#### 4.9 Set-off

By acceptance of the CCDS, each CCDS holder will be deemed to have waived any right of set-off or counterclaim that such CCDS holder might otherwise have against the Society in respect of or arising under the CCDS whether prior to or in a winding-up or dissolution. Notwithstanding the preceding sentence, if any of the rights and claims of any CCDS holder in respect of, or arising under, the CCDS are discharged by set-off, such CCDS holder will immediately pay an amount equal to the amount of such discharge to the Society or, if applicable, the administrator, receiver, liquidator or other insolvency official appointed with primary responsibility for the winding-up or dissolution of the Society and, until such time as payment is made, will hold a sum equal to such amount on trust for the Society or, if applicable, such administrator, receiver, liquidator or other insolvency official (as the case may be). Accordingly, such discharge will be deemed not to have taken place.

### 5. DISTRIBUTIONS

#### 5.1 Declaration of Distributions

The Board may, in its sole and absolute discretion, from time to time declare Periodic Distributions (**Distributions**, which term shall include any Interim Distribution and any Final Distribution each as defined below) in respect of the CCDS. With respect to any given Financial Year of the Society, the Board may declare an interim Distribution (an **Interim Distribution**) during such Financial Year and/or a final Distribution (a **Final Distribution**) in respect of such Financial Year.

A Distribution (or any part thereof) may be declared unconditionally or subject to satisfaction of such conditions as the Board may determine (which may include, without limitation, any consents or approvals which may be necessary for distribution of reserves of the Society).

If an Interim Distribution is declared during any Financial Year, it will (subject to satisfaction of the relevant conditions to payment, if any) be paid on 20 February in such Financial Year and if a Final Distribution is declared in respect of any Financial Year, it will (subject to satisfaction of the relevant conditions to payment, if any) be paid on 20 August falling in the Financial Year immediately following the Financial Year in respect of which the Final Distribution is declared, provided that if any such date is not a Business Day, such Interim Distribution or Final Distribution (as the case may be) will be paid on the immediately following Business Day (the **Distribution Payment Dates**).

The Board shall, at its sole discretion, be entitled from time to time to change the Distribution Payment Date for the payment of Final Distributions to a date which the Board considers appropriate, including, without limitation, if at any time the Society changes its accounting reference date (provided that such new Distribution Payment Date shall fall not more than five months following the end of the financial year in respect of which the relevant Final Distribution is declared), and the Distribution Payment Date for the payment of Interim Distributions shall at the same time be changed to the date falling six months prior to such date. Any new Distribution Payment Dates so determined will be promptly notified to CCDS holders in accordance with Condition 14 and published on the website of the Society (or, if this is not possible, via the Luxembourg Stock Exchange website ([www.bourse.lu](http://www.bourse.lu)) or a regulatory information service as may be recognised by any stock exchange on which the CCDS are for the time being listed).

#### 5.2 Distributions discretionary

The Board shall have full discretion at all times whether or not to declare any Interim Distribution or Final Distribution. Interim Distributions and Final Distributions are independent, and accordingly

whether or not the Board declares an Interim Distribution during any Financial Year shall have no effect or bearing on the Board's discretion whether or not to declare a Final Distribution in respect of that Financial Year (save that the amount of the Final Distribution (if any) declared in respect of a Financial Year shall not, when aggregated with any Interim Distribution paid during that Financial Year, exceed the Cap provided in Condition 5.5). If, at any time, the Board elects not to declare any Interim Distribution or Final Distribution, no Distribution or other amount in respect of the relevant period shall accumulate to CCDS holders or be payable at any time thereafter, and CCDS holders shall have no right to any Distribution or other amount in respect of such period, whether in a winding-up or dissolution of the Society or otherwise.

Notwithstanding the discretion of the Board referred to above, if the Supervisory Authority, by notice in writing to the Society, requires the Society not to declare any Distributions on the CCDS at any time or whilst any specified circumstances subsist or during a specified period, the Board shall not declare any Distributions until such time as the Supervisory Authority authorises it to resume Distributions on the CCDS, such circumstances cease to subsist or, as the case may be, expiration of the specified period.

### **5.3 Conditional Distributions**

If a Distribution (or any part thereof) is declared subject to the satisfaction of one or more conditions and any such condition is not satisfied on or prior to the relevant Distribution Payment Date, such Distribution (or, as the case may be, the part of such Distribution subject to the relevant condition) shall not accumulate to CCDS holders or be payable at any time thereafter, and CCDS holders shall have no right to such Distribution (or, as the case may be, the conditional part thereof) whether in a winding-up or dissolution of the Society or otherwise.

### **5.4 Distributions payable out of Distributable Items**

Distributions will be paid out of Distributable Items, and the Board shall not declare a Distribution that is greater than the amount of Distributable Items available for payment of such Distribution.

If the Distribution is to be paid entirely out of the Society's profits available for distribution, such payment is subject to the discretion of the Board. To the extent that the Distribution is to be paid from the Society's reserves, such payment is subject to the discretion of the Board and applicable legal and regulatory requirements relevant to making payments from the reserves.

### **5.5 Cap on Distributions**

The total Distribution paid on each CCDS in respect of any given Financial Year of the Society (being the aggregate of the Interim Distribution (if any) paid during such Financial Year and the Final Distribution (if any) paid in respect of such Financial Year) shall not exceed the prevailing Periodic Distributions Cap determined in accordance with the Rules (the **Cap**). The Cap prevailing from time to time in respect of the CCDS shall be published on the Society's website.

*The Rules provide that the initial Cap, which would have been applicable to Distributions in respect of the Financial Year to 31 March 2015 had CCDS been in issue during that Financial Year, was £15 per CCDS, and that (subject as stated below) in respect of each subsequent Financial Year the Cap will be adjusted for inflation by reference to the United Kingdom Consumer Price Index (overall index, 2005=100) (CPI) published by the Office for National Statistics (or any successor to that index). Such adjustment will be made by applying the CPI annual inflation percentage published by the Office for National Statistics in its statistical bulletin for the last full calendar month of the Financial Year in respect of which the Distributions are payable (being the percentage increase or decrease over the twelve months to and including that month) to the prevailing Cap.*

*The prevailing Cap in respect of the Financial Year to 31 March 2017 is £15.42. For illustrative purposes only (as the Board is not intending to declare any Distributions in respect of the Society's financial year to 31 March 2018), the Cap on Distributions for the financial year to 31 March 2018 will be determined by applying the Consumer Prices Index annual inflation percentage published by the Office for National Statistics in its statistical bulletin for March 2018 to the prevailing Cap in respect of the financial year to 31 March 2017 of £15.42.*

*If the CPI ceases to be published and no direct successor or replacement index is published, the Board shall be entitled to determine an appropriate replacement index for determining future inflation-based adjustments to the Cap, and shall have sole discretion to determine any modifications to the method of determining inflation-based adjustments to the Cap during the transition from CPI to the replacement index. The Society shall in each year determine the adjustment to the Cap promptly following publication of the relevant CPI (or successor or replacement index) data by the Office for National Statistics (or such successor or other organisation as may be responsible for publishing official data with respect to the relevant index) and will notify the Members of the Society of the adjusted Cap not later than at the first Annual General Meeting following publication of the relevant data.*

*In the event that adjustment of the Cap in the manner described above would prejudice the regulatory capital treatment of the CCDS, the Society will disapply those adjustment provisions and the Cap will revert to £15 per CCDS.*

## **5.6 Distribution due and payable following declaration**

Once declared, a Distribution will be due and payable by the Society on the relevant Distribution Payment Date, provided that any Distribution (or any part thereof) that is stated to be conditional as aforesaid will become due and payable on the relevant Distribution Payment Date only if the relevant conditions are satisfied on or prior to such Distribution Payment Date.

## **5.7 Non-declaration not default**

Neither a decision by the Board not to declare a Distribution (whether an Interim Distribution or a Final Distribution) at any time, nor non-payment of any Distribution (or any part thereof) in respect of which a relevant condition to payment of such Distribution (or such part) has not been satisfied on or before the relevant Distribution Payment Date, shall constitute a default by the Society under the CCDS for any purpose, and neither such event shall entitle CCDS holders to petition for the winding-up or dissolution of the Society.

## **5.8 Notice of Distribution**

Following determination by the Board whether any Interim Distribution or Final Distribution shall be declared, the Society will publish an announcement confirming (a) the amount (if any) of such Distribution, expressed as an amount per CCDS and (b) whether the Distribution (or any part thereof) is conditional and, if so, the relevant condition(s).

If the Board declares a Distribution which is, in whole or in part, conditional and one or more relevant conditions have not been satisfied on or before the relevant Distribution Payment Date, the Society will promptly publish an announcement confirming that such condition(s) have not been satisfied and that, accordingly, the Distribution (or the relevant part thereof) subject to such condition(s) is not, and shall not become, due and payable.

## **5.9 Distribution Policy**

The Society will from time to time publish on its website a distribution policy (the **Distribution Policy**) setting out the Board's expectations as regards the declaration of Distributions and certain factors which the Board may consider when determining whether or not to declare a Distribution and, if



so, the amount of such Distribution. Upon any change in the policy, the Society shall promptly publish the revised Distribution Policy on its website.

The Distribution Policy may give an indication of the Board's current expectations with respect to declaration of Distributions (the **Indication**). Any Indication will not be binding on the Board or the Society and the Board shall (subject to there being available sufficient Distributable Items) have absolute discretion to declare a Distribution which is higher (subject to the Cap) or lower than the Indication or to determine that no Distribution shall be declared in respect of the relevant period. The Board will have regard to a range of factors including those set out in the Distribution Policy and must satisfy itself that the declaration of any Distribution is consistent with maintaining the financial strength of the Society.

*The Distribution Policy as at the date of these Listing Particulars is summarised at paragraph 3 "Distribution Policy in respect of the CCDS" of "Part V: – Reasons for Offer, Use of Proceeds and CCDS Distribution Policy" of these Listing Particulars.*

## **6. PAYMENTS**

### **6.1 Payment by cheque or transfer**

Subject as follows, all payments in respect of the CCDS will be made by sterling cheque drawn on a bank or building society in the UK, posted on the Business Day immediately preceding the relevant due date for payment and made payable to the CCDS holder appearing in the CCDS Register in respect of the CCDS of which it is the holder at the close of business on the fifteenth day before the relevant due date (the **Record Date**) at the addresses shown in the CCDS Register on the Record Date, or in such other manner as the Principal Paying Agent shall agree with the Society.

Upon application of the CCDS holder to the Society, in the form from time to time prescribed by the Society, not less than 10 days before the due date for any payment in respect of its CCDS, the payment may be made by transfer on the due date for payment or, if such date is not a Business Day, on the immediately following Business Day, to a sterling account maintained by the relevant CCDS holder with a bank or building society in the UK.

*Notwithstanding this Condition 6.1, all payments in respect of CCDS held through Clearing System accounts will be credited to the cash accounts of Accountholders in each Clearing System in accordance with the relevant Clearing System's rules and procedures. Each investor holding beneficial interests in the CCDS through a Clearing System must look solely to the relevant Accountholder through which it holds its CCDS for its share of each payment so made. For so long as all CCDS are held in the Clearing Systems, the Record Date shall be determined in accordance with this Condition 6.1, save that the words "fifteenth day" shall be deemed to be replaced with "ICSD Business Day", which means a day on which the Clearing Systems are open for business.*

### **6.2 Payments subject to applicable laws**

Payments in respect of the CCDS will be subject in all cases to (i) any fiscal or other laws and regulations applicable thereto in the place of payment and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the **Code**) or otherwise imposed pursuant to Sections 1471 through 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or any law implementing an intergovernmental approach thereto or any other applicable law.

In the event that a withholding or deduction is required to be made under applicable law or regulation, the Society will cause the requisite amount to be withheld or deducted and CCDS holders will be entitled to receive only the balance of the relevant Distribution following such withholding or deduction.

*On the basis of United Kingdom tax law and practice prevailing as at the date of these Listing Particulars, all payments of Distributions in respect of the CCDS are expected to be made without withholding or deduction for or on account of any present or future taxes or duties of whatever nature imposed or levied by or on behalf of the UK or any political subdivision or any authority thereof or therein having power to tax.*

### **6.3 Partial payments**

If any amount due on the CCDS is not paid in full, the Registrar will annotate the CCDS Register of the amount in fact paid.

## **7. PRESCRIPTION**

Any amounts payable in respect of CCDS in respect of which no cheque or warrant has been cashed and no payment claimed shall cease to be payable after 12 years from the due date and shall revert to the Society.

## **8. NO REDEMPTION; PURCHASES**

### **8.1 No redemption**

The CCDS constitute permanent non-withdrawable deferred shares (as defined in the Act) in the Society and have no maturity date. The Society has neither an obligation nor any right to redeem or, save following a purchase as referred to in Condition 8.2, cancel the CCDS and CCDS holders do not have any right to require the Society to redeem, purchase or cancel the CCDS.

### **8.2 Purchases**

The Society may, in its sole discretion but subject to Condition 8.3, at any time purchase CCDS in the open market or otherwise at any price. CCDS so purchased may, at the option of the Society, be held, re-issued and/or re-sold or surrendered to the Registrar for cancellation.

Subsidiaries of the Society shall not be permitted to purchase and hold CCDS for their own account or that of the Society, and any such purchase shall be deemed to be a purchase by the Society for immediate cancellation. Nothing in the previous sentence shall prohibit a subsidiary of the Society from purchasing or holding CCDS in its capacity as personal representative, agent or trustee for or on behalf of, or for the benefit of, a person other than the Society or a subsidiary of the Society, and any such purchase shall not be deemed to be a purchase by the Society (for immediate cancellation or otherwise).

### **8.3 Purchases subject to supervisory consent**

Any purchase of CCDS by the Society will, if so required by the Supervisory Authority, the prudential rules applicable to the Society or any laws or regulations applicable to deferred shares of the Society at the relevant time, be conditional upon the Society having duly notified the Supervisory Authority of its intention to purchase the CCDS and the Supervisory Authority having consented, or, if applicable, within any applicable period not having objected, to such purchase.

## **9. REPLACEMENT OF CCDS CERTIFICATES**

A CCDS holder who has lost a CCDS Certificate shall immediately give notice in writing of such loss to the Society at its principal office and to the Registrar and Principal Paying Agent at its specified office. If a CCDS Certificate is damaged or alleged to have been lost, stolen or destroyed, a new CCDS Certificate representing the same CCDS shall be issued by the Registrar, on behalf of the Society, to the CCDS holder upon request, subject to delivery up of the old CCDS Certificate or (if alleged to have

been lost, stolen or destroyed) subject to compliance with such conditions as to evidence and indemnity as the Society and the Registrar may think fit and to payment of any exceptional expenses of the Society and the Registrar incidental to any investigation of the evidence of such alleged loss, theft or destruction. The duplicate CCDS Certificate will be made available at the specified office of the Registrar.

## **10. SUCCESSION AND TRANSFERS**

### **10.1 Amalgamation or transfer under section 93 or 94 of the Act**

Upon an amalgamation by the Society with another building society under section 93 of the Act or a transfer of all or substantially all of its engagements to another building society under section 94 of the Act, the CCDS shall become deferred shares in the amalgamated or transferee building society, as appropriate (the **Resulting Society**), having such terms and conditions as are necessary to ensure that both the CCDS and any other deferred shares which, prior to such amalgamation or transfer, constituted Common Equity Tier 1 Capital of the other society, shall constitute Common Equity Tier 1 Capital of the Resulting Society and, subject thereto, in all material respects identical to the terms of the CCDS, all as determined by an independent financial adviser (having regard to such factors as it considers appropriate) appointed by the Society in its sole discretion.

*It may be necessary, upon an amalgamation by the Society with another building society or a transfer of all or substantially all of its engagements to another building society as envisaged by Condition 10.1, for the terms of the CCDS and/or the rules of the Resulting Society to be amended in certain respects and/or for certain adjustments to be made to the prevailing Core Capital Contribution Proportion, Average Principal Amount and/or Cap on Distributions and, where applicable, the formulae for calculating the same. With a view to minimising the financial impact of such amendments and adjustments on CCDS holders, it is the intention of the Society that, if and to the extent that the Society has control over such matters, any such amendments and adjustments should be limited to the minimum necessary in order to ensure that the CCDS and any other deferred shares of the other society which, prior to such amalgamation or transfer, constituted Common Equity Tier 1 Capital of the other society, shall constitute Common Equity Tier 1 Capital of the Resulting Society.*

### **10.2 Transfer of business under section 97 of the Act**

Upon a transfer by the Society of the whole of its business in accordance with section 97 of the Act to a company (a **Successor Entity**, which expression includes a subsidiary of a mutual society as referred to in the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 as amended (the **Mutual Societies Transfers Act**)) the Successor Entity will, in accordance with section 100(2)(a) of the Act, as from the vesting date, assume a subordinated liability (a **Subordinated Deposit**) to each holder of CCDS, which Subordinated Deposit shall be applied on the vesting date (or as soon as reasonably practicable thereafter), on behalf of the CCDS holder, in the subscription of such number of ordinary shares (which may or may not carry voting rights) in the Successor Entity or, if appropriate, any direct or indirect parent company of the Successor Entity, ranking *pari passu* in all respects with the then existing ordinary shares of such Successor Entity or such parent, as applicable, as have an aggregate market value immediately following such subscription as near as practicable to, but not less than, the market value of the CCDS immediately prior to the time of transfer of the business of the Society to the Successor Entity, as determined by an independent financial adviser (having regard to such factors as it considers appropriate, including recent trading prices if available) appointed by the Society in its sole discretion.

### **10.3 Basis of appointment of independent financial adviser**

Any independent financial adviser appointed pursuant to Condition 10.1 or 10.2 shall act as an expert and not as an arbitrator, and all fees, costs and expenses in connection with such appointment shall be borne by the Society. Any determination made in good faith by such independent financial adviser

pursuant to Condition 10.1 or 10.2 shall be binding on the Society, the Registrar and the CCDS holders. No independent financial adviser appointed pursuant to Condition 10.1 or 10.2 shall have any responsibility or liability whatsoever to any CCDS holder or to any other person in connection with any determination made by it in good faith pursuant to Condition 10.1 or 10.2.

#### **10.4 Failure to obtain a determination by independent financial adviser**

If, in circumstances which require an independent financial adviser to make any determination pursuant to Condition 10.1 or 10.2, the Society is unable to appoint such independent financial adviser, or the appointed independent financial adviser fails to make any necessary determination and the Society is unable to appoint an alternative or additional independent financial adviser to make such determination, the Society shall convene a meeting of the CCDS holders in accordance with Condition 12 in order for such holders to approve by resolution those determinations which remain to be made. Such approval may alternatively be obtained by way of a written resolution in accordance with Condition 12.7.

#### **10.5 Undertakings**

- (a) The Society undertakes to procure that any amalgamation or transfer referred to in Condition 10.1 or 10.2 will comply with the provisions of Condition 10.1 or, as the case may be, 10.2. The Society undertakes to use all reasonable endeavours to enter into such agreements, and to take such other reasonable steps, as are necessary to give effect to the provisions of this Condition 10 (including, but not limited to, the appointment, if applicable, of an independent financial adviser).
- (b) In connection with any amalgamation by the Society with another building society under section 93 of the Act or a transfer of all or substantially all of its engagements to another building society under section 94 of the Act as provided in Condition 10.1, the Society:
  - (i) shall, and shall use all reasonable endeavours to procure that the Resulting Society shall, comply with the rules of any competent authority, stock exchange and/or quotation system by or on which the CCDS are, for the time being, listed, traded and/or quoted; and
  - (ii) shall pay, or shall use all reasonable endeavours to ensure that Resulting Society pays, any taxes, stamp duty reserve taxes and capital, stamp, issue and registration duties payable in the UK arising on the issue and initial delivery of such deferred shares, but will not pay (and each CCDS holder as to itself will be required to pay) any other taxes, stamp duty reserve taxes and capital, stamp, issue and registration duties arising on or following the issue and initial delivery of such deferred shares pursuant to Condition 10.1.
- (c) In connection with any transfer by the Society of the whole of its business in accordance with section 97 of the Act to a company as provided in Condition 10.2, the Society:
  - (i) shall, and shall use all reasonable endeavours to procure that the Successor Entity shall, comply with the rules of any competent authority, stock exchange and/or quotation system by or on which the CCDS are, for the time being, listed, traded and/or quoted; and
  - (ii) shall pay, or shall use all reasonable endeavours to ensure that the terms upon which its business is transferred to the Successor Entity shall require the Successor Entity to pay, any taxes, stamp duty reserve taxes and capital, stamp, issue and registration duties payable in the UK arising on the issue and initial delivery of such ordinary shares, but will not pay (and each CCDS holder as to itself will be required to pay)

any other taxes, stamp duty reserve taxes and capital, stamp, issue and registration duties arising on or following the issue and initial delivery of such ordinary shares pursuant to Condition 10.2.

## **11. VARIATIONS OF THESE CONDITIONS**

- 11.1 Save as provided in Condition 11.5, these Conditions may only be varied by the Society with the consent in writing of the CCDS holders in accordance with Condition 12.7 or with the sanction of a resolution passed at a separate meeting of the CCDS holders held in accordance with Condition 12 (all as more fully described in Schedule 3 to the Agency Agreement).
- 11.2 These Conditions do not limit the rights of Members of the Society to amend the Rules.
- 11.3 The Society undertakes not to initiate any amendment to the Rules that is both (a) inconsistent with the provisions of these Conditions and (b) materially prejudicial to the interests of the CCDS holders in that capacity.
- 11.4 The provisions of Condition 11.2 and any amendment to the Rules or any resolution of Members of the Society (in either case whether such amendment or resolution is initiated by the Society or by one or more of its Members) shall not:
- (a) limit any rights of any CCDS holder to bring an action against the Society for breach of contract in circumstances where the Society is in breach of these Conditions, and furthermore any CCDS holder shall be entitled to bring an action against the Society as if there had been a breach of contract (such that a CCDS holder may sue for a liquidated sum equal to its loss) in circumstances where an amendment has been made to the Rules or any resolution of Members of the Society has been passed which is materially prejudicial to the holders of CCDS as a class and which would have been a breach of these Conditions had such amendment been instituted by the Society; or
  - (b) afford the Society any defence to any claim made in any action referred to under (a) above,
- provided, however, that no CCDS holder shall be entitled to bring an action against the Society under (a) above, and the Society shall have a valid defence to any such action under (b) above, if the holders of CCDS have at any time passed a resolution in accordance with Condition 12 (whether at a duly convened meeting of the holders of CCDS or by way of written resolution) approving, ratifying and/or consenting to the relevant amendment to the Rules or the relevant Member resolution, as the case may be.
- 11.5 If, at any time, a Regulatory Event occurs, the Society may, without the need for the consent of the holders of the CCDS, upon not less than 30 nor more than 90 days' notice to holders of the CCDS in accordance with Condition 14, vary the terms of the CCDS so that they remain or (as the case may be) become capable of qualifying in full as Common Equity Tier 1 Capital of the Society, provided that:
- (a) the terms of the CCDS, as so varied, are not materially less favourable to the CCDS holders than the terms immediately prior to such variation (as reasonably determined by the Society in good faith in consultation with an independent adviser of recognised standing, in which regard a certification to such effect shall be signed by two Directors of the Society and made available to holders for inspection); and
  - (b) if the CCDS were admitted to listing and/or trading on any stock exchange immediately prior to such variation, the CCDS continue to be admitted to listing and/or trading on the same stock exchange or on another stock exchange selected by the Society.

Any such variation, which will be binding on all CCDS holders, will be subject to compliance with prevailing Capital Rules at such time and, if then required by the Supervisory Authority or the Capital Rules, be conditional upon the Society having duly notified the Supervisory Authority of its intention to vary the terms of the CCDS and the Supervisory Authority having consented, or (if applicable) within any applicable period not having objected, to such variation.

## **12. MEETINGS OF THE CCDS HOLDERS**

### **12.1 Convening the meeting, notice and quorum**

The Society alone may at any time convene a separate meeting of the CCDS holders. Every meeting shall be held at such place as the Society may approve.

At least 21 clear days' notice specifying the hour, date and place of the meeting shall be given to the CCDS holders entered in the CCDS Register 35 days prior to the date specified for the meeting, such notice to be given in accordance with Condition 14. The notice shall specify generally the nature of the business to be transacted at the meeting and the terms of any resolution to be proposed to alter these Conditions.

Any person (who may, but need not, be a CCDS holder) nominated in writing by the Society shall be entitled to take the chair at every meeting but if no nomination is made or if at any meeting the person nominated shall not be present within 15 minutes after the time appointed for holding the meeting, the CCDS holders present shall choose one of their number who is present to be chairman.

At any meeting one or more persons present in person or by proxy and holding or representing in aggregate not less than one-third of the number of CCDS for the time being Outstanding shall form a quorum for the transaction of business and no business (other than the choosing of a chairman) shall be transacted at any meeting unless the requisite quorum shall be present at the commencement of business. Every question submitted to the meeting (other than the choosing of a chairman which will be decided by a simple majority) shall be decided by a poll of one or more persons present and holding CCDS or being proxies and representing in aggregate not less than three-quarters of the number of the CCDS represented at such meeting voting in favour of such question.

### **12.2 Adjournment**

If within half an hour after the time appointed for any meeting a quorum is not present, the meeting shall stand adjourned for such period, being not less than 14 days nor more than 42 days and at such place as may be appointed by the chairman and if at the adjourned meeting a quorum shall not be present within half an hour from the time appointed for the adjourned meeting, the CCDS holders present in person or by proxy at the adjourned meeting shall be a quorum.

The chairman may with the consent of (and shall if directed by a resolution of) the meeting adjourn any meeting from time to time and from place to place but no business shall be transacted at any adjourned meeting other than business left unfinished or not reached at the meeting from which the adjournment took place.

Notice of any adjourned meeting shall be given in the same manner as notice of an initial meeting but as if 10 were substituted for 21 in Condition 12.1.

### **12.3 Conduct of business of the meeting**

Any director or officer of the Society and its professional advisers may attend and speak at any meeting of the CCDS holders. Save as provided above, no person shall be entitled to attend and speak nor shall any person be entitled to vote at any such meeting unless it is a CCDS holder or is a proxy thereof.

A poll shall be taken in such manner as the chairman directs and the result of the poll shall be deemed to be the resolution of the meeting.

At any meeting every CCDS holder or proxy who is present shall have one vote for each CCDS held or, as the case may be, in respect of which it is a proxy.

#### **12.4 Proxies**

A CCDS holder entitled to attend a separate meeting of the CCDS holders:

- (a) may appoint one person (whether or not a CCDS holder) as its proxy to attend and, on a resolution, to vote at such meeting in its place; and
- (b) may direct the proxy how to vote at the meeting.

A proxy shall be appointed in the manner provided in Schedule 3 to the Agency Agreement.

#### **12.5 Effect of resolution**

Any resolution passed at a meeting duly convened and held in accordance with the provisions of this Condition 12 shall be binding upon all the CCDS holders whether or not present at the meeting and whether or not voting and each of them shall be bound to give effect to the resolution accordingly and the passing of any resolution shall be conclusive evidence of the circumstances justifying the passing of the resolution.

#### **12.6 Other matters**

Minutes of all resolutions and proceedings at every meeting shall be made and duly entered in books to be from time to time provided for that purpose by the Society and any minutes purporting to be signed by the chairman of the meeting at which resolutions were passed or proceedings had shall be conclusive evidence of the matters contained in the minutes and until the contrary is proved every meeting in respect of the proceedings of which minutes have been so made and signed shall be deemed to have been duly held and convened and all resolutions passed or proceedings had to have been duly passed or had.

The accidental omission to send notice of a separate meeting or to send any document required to be sent with the notice or otherwise before the meeting to, or the non-receipt of notice of a separate meeting or any such document as aforesaid by, any person entitled to receive notices or documents shall not invalidate the proceedings at that meeting.

#### **12.7 Written resolution**

A resolution may also be passed, without the need for a meeting of CCDS holders, by way of a resolution in writing signed by or on behalf of CCDS holders holding in aggregate not less than three-quarters of the number of CCDS for the time being Outstanding. Such written resolution may be contained in one document or several documents in like form each signed by or on behalf of one or more such CCDS holders. Any written resolution passed shall be binding upon all the CCDS holders whether or not signing the written resolution and each of them shall be bound to give effect to the resolution accordingly.

#### **12.8 Notice**

Notice of any resolution duly passed by the CCDS holders, whether at a meeting of CCDS holders or by written resolution, shall be given in accordance with Condition 14 by the Society within 14 days of

the passing of the resolution, provided that failure to give such notice shall not invalidate the resolution.

### 13. FURTHER ISSUES

The Society shall be at liberty from time to time, without the consent of the CCDS holders, to create and issue at any price further Deferred Shares ranking *pari passu* in all respects and so that the same shall be consolidated and form a single series with the Outstanding CCDS (**Additional CCDS**).

The Society shall be at liberty from time to time, without the consent of the CCDS holders, to create and issue, at any price, Deferred Shares upon such other terms of issue as the Society may at the time of issue determine, provided that the Society shall not issue any Core Capital Deferred Shares (within the meaning of the Rules) other than Additional CCDS.

### 14. NOTICES

All notices regarding the CCDS shall be valid if sent by post to the CCDS holders at their respective addresses in the CCDS Register. Any such notice shall be deemed to have been given on the second Business Day following the mailing of such notice. For so long as the CCDS are listed or admitted to trading on any stock exchange, such notice shall also be made available in any other manner required by the rules of such stock exchange then in effect.

### 15. RIGHTS OF THIRD PARTIES

No person shall have any right to enforce any term or condition of the CCDS under the Contracts (Rights of Third Parties) Act 1999.

### 16. GOVERNING LAW

The rights and obligations in respect of the CCDS and any non-contractual obligations arising out of or in connection with the CCDS are governed by, and shall be construed in accordance with, English law.

*Section 85 of, and Schedule 14 to, the Act provide that no court other than the High Court of Justice in England shall have jurisdiction to hear and determine disputes between a building society and a member or a representative of a member in that capacity in respect of any rights or obligations arising from the rules of a building society or the Act. Under various other enactments, the High Court is empowered to transfer cases over which it has jurisdiction to the County Court.*

### 17. DEFINITIONS

For the purpose of these Conditions:

**Act** has the meaning given in Condition 1.2(a).

**Additional CCDS** has the meaning given in Condition 13.

**Agency Agreement** has the meaning given in the preamble to these Conditions.

**Average Principal Amount** has the meaning given in Condition 4.5.

**Board** means the Board of Directors of the Society.

**Business Day** means a day on which commercial banks and foreign exchange markets settle payments and are open for general business (including dealings in foreign exchange and foreign currency deposits) in London.



**Cap** has the meaning given in Condition 5.5.

**Capital Rules** means the applicable rules of the Supervisory Authority (as amended or replaced from time to time) and any other rules or regulations relating to the capital adequacy or prudential requirements to which the Society and its group are subject from time to time, and shall include (without limitation) any measures applicable to the Society which are intended to implement the reforms contained in “*Basel III: A global regulatory framework for more resilient banks and banking systems*” published by the Basel Committee on Banking Supervision in December 2010, including (without prejudice to the generality of the foregoing) *Directive 2013/36/EU of the European Parliament and of the Council of 26 June 2013 on access to the activity of credit institutions and the prudential supervision of credit institutions and investment firms, amending Directive 2002/87/EC and repealing Directives 2006/48/EC and 2006/49/EC* (commonly referred to as the **Capital Requirements Directive IV** or **CRD IV**), *Regulation (EU) No 575/2013 of the European Parliament and of the Council of 26 June 2013 on prudential requirements for credit institutions and investment firms and amending Regulation (EU) No 648/2012* (commonly referred to as the **Capital Requirements Regulation** or **CRR**), applicable regulatory technical standards published by the European Banking Authority and adopted by the European Commission (by way of regulation or otherwise) and any rules promulgated in connection with any of the foregoing.

**CCDS** has the meaning given in the preamble to these Conditions.

**CCDS Certificate** has the meaning given in Condition 2.3.

**CCDS holder** means a person whose name and address is entered in the CCDS Register as the holder of CCDS, and references to a **holder** of CCDS shall be construed accordingly.

**CCDS Register** means the records of the Society maintained by the Registrar constituting the register of members for the purposes of the CCDS.

**Common Equity Tier 1 Capital**, at any time, has the meaning ascribed thereto (or to any equivalent term) at such time in the Capital Rules.

**Conditions** means these conditions of issue of the CCDS, and references to a numbered Condition shall be construed accordingly.

**Conversion Benefits** has the meaning given in Condition 1.3.

**Core Capital Contribution Proportion** has the meaning given in Condition 4.4.

**Core Capital Contribution Share** has the meaning given in Condition 4.4.

**Core Capital Deferred Share** has the meaning given in the Rules (except where used in the preamble to these Conditions).

**Deferred Shares** has the meaning given in the Rules.

**Deferred Shares Register** has the meaning given in the Rules.

**Determination Time** or **DT** has the meaning given in Condition 4.4.

**Distributable Items** means, in respect of the payment of a Distribution at any time, those profits and reserves (if any) of the Society which are available, in accordance with applicable law and regulation for the time being, for the payment of such Distribution.

*As at the date of these Listing Particulars, Article 4(1)(128) of the Capital Requirements Regulation provides as follows: “distributable items” means the amount of the profits at the end of the last*

*financial year plus any profits brought forward and reserves available for that purpose before distributions to holders of own funds instruments less any losses brought forward, profits which are non-distributable pursuant to provisions in legislation or the institution's bye-laws and sums placed to non-distributable reserves in accordance with applicable national law or the statutes of the institution, those losses and reserves being determined on the basis of the individual accounts of the institution and not on the basis of the consolidated accounts."*

**Distribution Payment Dates** has the meaning given in Condition 5.1, and **Distribution Payment Date** shall be construed accordingly.

**Distribution Policy** has the meaning given in Condition 5.9.

**Distributions** has the meaning given in Condition 5.1, and **Distribution** shall be construed accordingly.

**Final Distribution** has the meaning given in Condition 5.1.

**Financial Year** has the meaning given in the Rules.

**Interim Distribution** has the meaning given in Condition 5.1.

**Liabilities** means (i) the claims of all creditors (including, without limitation, creditors in respect of subordinated liabilities) of the Society and (ii) the claims of all other Shareholding Members (as defined in the Rules) of the Society in respect of the amounts paid up on their shares (including Deferred Shares, other than Core Capital Deferred Shares), in each case including any principal amount, any interest (including post-petition interest) thereon and any other amounts owing thereon, but excluding (x) any actual, prospective or contingent claims to participate in a distribution of Surplus of the Society and (y) any claims in respect of declared, unconditional and unpaid Distributions in accordance with Condition 4.8 and claims ranking or expressed to rank *pari passu* therewith.

**Member** has the meaning given in the Rules.

**Minimum Transfer Amount** has the meaning given in Condition 2.2.

**Nominal Amount** has the meaning given in Condition 2.1.

**Outstanding** means, in relation to the CCDS, all the CCDS issued other than:

- (a) those CCDS which have been cancelled in accordance with Condition 8; and
- (b) any global CCDS Certificate to the extent that it shall have been exchanged for definitive CCDS Certificates pursuant to its provisions;

PROVIDED THAT for each of the following purposes, namely:

- (i) the right to attend and vote at any meeting of the CCDS holders or any of them or to pass a resolution by way of written resolution in place of a meeting and any direction or request by CCDS holders;
- (ii) the determination of how many and which CCDS are for the time being Outstanding for the purposes of Condition 12 and paragraphs 8, 9, 21 and 22 of Schedule 3 to the Agency Agreement;
- (iii) any discretion, power or authority (whether granted under these Conditions, the Rules or applicable laws) which any person is required, expressly or impliedly, to exercise in or by reference to the interests of the CCDS holders or any of them; and

- (iv) the determination by any person whether any event, circumstance, matter or thing is, in its opinion, materially prejudicial to the interests of the CCDS holders or any of them,

those CCDS (if any) which are for the time being held by or on behalf of or for the benefit of the Society, any subsidiary of the Society or any holding company of the Society or any other subsidiary of such holding company, in each case as beneficial owner, shall (unless and until ceasing to be so held) be deemed not to remain Outstanding;

AND FURTHER PROVIDED THAT for the purposes of Conditions 4.2, 4.3(a), 4.4(a) and 4.4(b), all CCDS held by the Society in its treasury function at the Relevant Time (but, for the avoidance of doubt, not at any other Determination Time) shall be deemed to be cancelled at the Relevant Time (such cancellation to be reflected in the determination of the Core Capital Contribution Proportion at the Relevant Time) and not to be or remain Outstanding for such purposes.

*The effect of the second proviso above is that CCDS held by the Society as beneficial owner shall be treated as being cancelled upon a winding-up or dissolution of the Society and accordingly shall not be Outstanding for the purposes of any calculation of the Core Capital Contribution Share, and accordingly no claim shall be made in respect of those CCDS so held in the winding-up or dissolution of the Society.*

**Periodic Distributions** has the meaning given in the Rules.

**Periodic Distributions Cap** has the meaning given in the Rules.

**Principal Amount** has the meaning given in Condition 2.1.

**Principal Paying Agent** has the meaning given in the preamble to these Conditions.

**Record Date** has the meaning given in Condition 6.1.

**Registrar** has the meaning given in the preamble to these Conditions.

a **Regulatory Event** will occur if there is a change (which has occurred or which the Supervisory Authority considers to be sufficiently certain) in the regulatory classification of the CCDS such that the CCDS or any part of them are, or are likely to be, excluded from the Common Equity Tier 1 Capital of the Society (whether on an individual or consolidated basis).

**Relevant Regulators** means the Supervisory Authority and/or the Financial Conduct Authority (or any successor thereto) as required in the circumstances.

**Relevant Time** has the meaning given in Condition 4.3.

**Rules** has the meaning given in the preamble to these Conditions.

**Supervisory Authority** means the Prudential Regulation Authority (or any successor or other authority having primary supervisory authority with respect to prudential matters in relation to the Society).

**Surplus** has the meaning given in Condition 4.2.

## OVERVIEW OF PROVISIONS RELATING TO THE CCDS WHILE REPRESENTED BY THE GLOBAL CCDS CERTIFICATE

The following is a summary of the provisions to be contained in the Agency Agreement and in the global certificate representing all the CCDS upon issue (the **Global CCDS Certificate**) which will apply to, and in some cases modify the effect of, the Conditions while the CCDS are represented by the Global CCDS Certificate:

### 1. EXCHANGE OF THE GLOBAL CCDS CERTIFICATE AND REGISTRATION OF TITLE

Registration of title to CCDS in a name other than that of the Nominee will be permitted only if all Clearing Systems have closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or do in fact do so.

Thereupon, the Nominee (acting on the instructions of one or more of the Accountholders (as defined below)) may give notice to the Society of its intention to exchange the Global CCDS Certificate for definitive CCDS Certificates on or after the Exchange Date (as defined below). References herein to **Accountholders** are to each person (other than a Clearing System) who is for the time being shown in the records of a Clearing System as the holder of a particular number of CCDS (in which regard any certificate or other document issued by that Clearing System as to the number of CCDS standing to the account of any person shall be conclusive and binding for all purposes).

On or after the Exchange Date, the Nominee may surrender the Global CCDS Certificate to or to the order of the Registrar. In exchange for the Global CCDS Certificate, the Registrar will deliver, or procure the delivery of, definitive CCDS Certificates printed in accordance with any applicable legal and stock exchange requirements and in or substantially in the form set out in the Agency Agreement. On exchange of the Global CCDS Certificate, the Society will procure that it is cancelled and, if the Nominee so requests, returned to the Nominee together with any relevant definitive CCDS Certificates.

For these purposes, **Exchange Date** means a day specified in the notice requiring exchange falling not less than 10 days after that on which such notice is given and being a day on which banks are open for general business in the place in which the specified office of the Registrar is located.

### 2. PAYMENTS

Payments due in respect of CCDS represented by the Global CCDS Certificate shall be made by the Registrar or the Principal Paying Agent to or to the order of the Nominee. A record of each payment made in respect of CCDS represented by the Global CCDS Certificate will be endorsed on the appropriate part of the schedule to the Global CCDS Certificate by or on behalf of the Registrar, which endorsement shall be *prima facie* evidence that such payment has been made in respect of the CCDS.

Payment by the Registrar or the Principal Paying Agent to or to the order of the Nominee as aforesaid will discharge the obligations of the Society in respect of the relevant payment under the CCDS. Each Accountholder must look solely to its Clearing System for its share of each payment made to or to the order of the Nominee, and each Beneficial Owner (as defined in paragraph 4 below) who is not itself an Accountholder must look solely to the relevant Accountholder through which it holds its CCDS for its share of each payment made to such Accountholder.

### 3. TRANSFERS

Transfers of book-entry interests in the CCDS will be effected through the records of the Clearing Systems and their respective direct and indirect participants in accordance with their respective rules and procedures.

The Minimum Transfer Amount prevailing from time to time, as determined in accordance with Condition 2.2, shall apply *mutatis mutandis* to transfers of book-entry interests in the CCDS. Accordingly, a transfer of book-entry interests in the CCDS will only be effected by the Clearing Systems if such transfer is in respect of a whole number of CCDS equal to or greater than the Minimum Transfer Amount prevailing at the time of the transfer.

*The CCDS are transferable in whole numbers, subject to the Minimum Transfer Amount, and not on the basis of principal amount. For example, an instruction to sell or purchase “100,000” CCDS in a Clearing System will be an instruction to sell or purchase (as the case may be) one hundred thousand CCDS (and not an instruction to sell or purchase £100,000 in principal amount of CCDS).*

*The Clearing Systems will not accept instructions to settle transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount. Accordingly, purported transfers of CCDS in amounts less than the prevailing Minimum Transfer Amount will be incapable of settlement. Investors in CCDS are responsible for ensuring that any trades they enter into in respect of the CCDS are capable of settlement; failure to do so may result in an investor breaching its contract of sale and purchase.*

#### 4. DISCLOSURE OF CCDS HOLDINGS

For so long as any CCDS are represented by the Global CCDS Certificate and such Global CCDS Certificate is registered in the name of the Nominee, the Society (or an agent on its behalf) may from time to time give notice (a **Compliance Notice**), in accordance with the usual procedures of the Clearing Systems, requiring Beneficial Owners and Intermediaries (each as defined below) to disclose to the Society (or to its appointed agent, which shall be bound to confidentiality by contract or by generally applicable law and regulation) such information (the **Compliance Information**) as the Society considers necessary in order for it to establish its continued compliance with its obligations under article 13 of the Grand Ducal Regulation dated 13 July 2007 relating to the holding of an official list for financial instruments, article 702 1.8 of the rules and regulations of the Luxembourg Stock Exchange (version 01/2018) and such equivalent rules (if any) under the listing rules of any other stock exchange on which the CCDS are, for the time being, listed or admitted to trading, in each case as amended or supplemented or replaced from time to time (together, the **Free Float Rules**, and references to the Luxembourg Stock Exchange being construed accordingly).

The Compliance Information to be provided will be specified in the relevant Compliance Notice, and may include (without limitation) (i) the legal name of the holder of any CCDS; (ii) the number of CCDS held by such person; (iii) whether, to its knowledge, such person has any connection with the Society or any Director of the Society or whether any other circumstance exists which would be relevant for the purpose of determining whether the requirements contained in the Free Float Rules are being met; and (iv) if that person acquired any CCDS after the Record Time (as defined below), the legal name of the person from whom it acquired such CCDS.

Each Beneficial Owner will be required to provide the specified Compliance Information as regards itself and its own holding of CCDS. Each Intermediary will be required to provide the specified Compliance Information both as regards (i) itself and its holdings of CCDS as Intermediary and (ii) to the best of its knowledge, the persons (whether Beneficial Owners or other Intermediaries) for whom it is acting as Intermediary and the CCDS which it holds for such persons.

The relevant Compliance Notice will specify, in addition to the nature of the Compliance Information to be disclosed, the reference date and time as at which holdings of CCDS must be disclosed (the **Record Time**), the period during which the relevant information must be disclosed (the **Disclosure Period**) and the procedure for providing such information (which is expected to be in accordance with the usual procedures of the Clearing Systems).

By acquiring and holding CCDS, each Beneficial Owner and Intermediary:

- (a) acknowledges that the provision of Compliance Information is mandatory, and undertakes promptly (and in any event within the Disclosure Period) following receipt of a Compliance Notice to provide to the Society (or to its appointed agent) all Compliance Information specified in such Compliance Notice;
- (b) authorises and empowers (without the need for any further action or authorisation) each Intermediary through which it holds CCDS to disclose, on its behalf, to the Society (or to its appointed agent) all Compliance Information specified in such Compliance Notice (to the extent that such information is available to such Intermediary); and
- (c) acknowledges that the Society may share such Compliance Information, on a strictly confidential basis and for the purpose only of assessing and evidencing its compliance with its obligations under the Free Float Rules, with its agents and its professional advisers (provided that such agents and advisers are bound to confidentiality by contract or by generally applicable law and regulation) and, if it so requests, the Luxembourg Stock Exchange (or such other competent authority as may from time to time be responsible for ensuring compliance with the Free Float Rules).

The Society undertakes that it will (i) use all Compliance Information obtained solely for the purpose of assessing and establishing its compliance with its obligations under the Free Float Rules, (ii) retain appropriate internal records in respect of such Compliance Information and keep such internal records and information confidential and will not use or disclose any Compliance Information obtained except as set out under (c) above or otherwise as may be required by applicable law and regulation.

As used herein:

**Beneficial Owners** means each person who for the time being (or, where appropriate, as at the relevant Record Time) holds any interests in CCDS for its own account (and not only as custodian or an Intermediary for another person); and

**Intermediary** means each Clearing System and each Accountholder, custodian, broker or other intermediary who for the time being (or, where appropriate, as at the relevant Record Time) holds interests in CCDS (as custodian or otherwise) for the account of another person (and **Intermediaries** shall be construed accordingly).

For these purposes, CCDS will be deemed to be held by a Beneficial Owner or an Intermediary if an interest in such CCDS is (or, where appropriate, was as at the relevant Record Time) credited to the account of such Beneficial Owner or Intermediary with a Clearing System (or to an account with an Intermediary which in turn holds such CCDS, either directly or indirectly through one or more further Intermediaries, in an account with a Clearing System) and references to **held**, **holds**, **holder**, **holding** or similar references shall be construed accordingly.

*The Free Float Rules require the Society to ensure that a sufficient number of CCDS are distributed to the public, and on an ongoing basis remain, in the hands of the public within the meaning of the Free Float Rules (commonly referred to as the 'free- float' listing requirement).*

## 5. NOTICES

For so long as the CCDS are represented by the Global CCDS Certificate and such Global CCDS Certificate is held on behalf of one or more Clearing Systems, notices may be given to the CCDS holders by delivery of the relevant notice to the relevant Clearing Systems for communication to the relevant Accountholders and Beneficial Owners in substitution for despatch and service as required by Condition 14. Such notice shall be deemed to have been given on the date of delivery of the notice to the relevant Clearing Systems for such communication.

## **6. MEETINGS; MEMBERSHIP RIGHTS WHILST THE CCDS ARE HELD THROUGH CLEARING SYSTEMS**

Save as permitted in paragraph 1 above, investors will hold their CCDS directly or indirectly through Accountholders with the Clearing Systems and will not themselves be entered on the CCDS Register as holder of the relevant CCDS. Instead, the holder entered on the CCDS Register for such CCDS shall be the Nominee and the relevant Accountholder's holding of interests in such CCDS will be recorded in the internal records of the relevant Clearing Systems.

This means that Accountholders and Beneficial Owners will not themselves be members of the Society and, accordingly, will not be entitled to vote at any general meeting of the members of the Society or in a postal ballot or to any other similar membership rights. Instead, the members' rights attaching to the CCDS held through the Clearing Systems will be held by the Nominee. Such Nominee will be entered in the CCDS Register as the holder of such CCDS, and will be entitled to exercise the voting and other members' rights attributable to such CCDS. Each member of the Society has one vote at any general meeting of the members of the Society. Accordingly, the Nominee will be entitled to exercise one vote at any such meeting, regardless of the number of CCDS held by it (and regardless also of the size and number of other relevant investments or interests (if any) conferring membership rights which the Nominee may have in the Society).

Given the difficulty of casting the single vote at a general meeting of the members of the Society in a manner which reflects the views of all Beneficial Owners of CCDS and the insignificance of that vote in the context of all the votes which may be cast by members of the Society, the Nominee has informed the Society that it does not intend to exercise its vote insofar as it relates to its holding of CCDS.

At a separate meeting of CCDS holders only, the Nominee will have one vote per CCDS and will act on the instructions of one or more Accountholders (who in turn will act on the direct or indirect instructions of Beneficial Owners holding through such Accountholders) received by it through the Clearing Systems. The Agency Agreement contains provisions relating to the convening and conduct of such meetings of CCDS holders. Those provisions include arrangements pursuant to which a Beneficial Owner will be able (i) to attend any such meeting and cast the votes attributable to its CCDS or (ii) otherwise to direct (including by way of electronic consents) how the votes attributable to its CCDS shall be cast at such meeting. For these purposes, notwithstanding the provisions of Condition 12.4(a), the Nominee shall be entitled to appoint one or more persons as its proxy or proxies to attend, speak and, on a resolution, vote at a meeting of CCDS holders. Each proxy shall be appointed in respect of such number of CCDS specified by the Nominee (provided that no two proxies can be appointed in respect of the same CCDS). The Agency Agreement also contains provisions for the passing of resolutions, without the need for a meeting of CCDS holders, by way of electronic consents communicated through the electronic communications systems of the relevant clearing system(s) by or on behalf of CCDS holders holding in aggregate not less than three-quarters of the number of CCDS for the time being Outstanding.

As Accountholders and Beneficial Owners will not be members of the Society, they will also not be entitled to any Conversion Benefits (including any rights to windfall payments) arising on a demutualisation or merger of the Society. Any Conversion Benefits arising on a demutualisation or merger of the Society will belong instead to the Nominee, as the registered holder of the CCDS in the CCDS Register. The Nominee will, on or prior to the date of issue of the CCDS, irrevocably agree to assign to a selected charity nominated by the Society pursuant to any scheme for charitable assignment established by the Society any Conversion Benefits.

## **7. RECORD DATE**

For so long as all CCDS are held in the Clearing Systems, the Record Date shall be determined in accordance with Condition 6.1 provided that the words "fifteenth day" shall be deemed to be replaced

with “ICSD Business Day”. **ICSD Business Day** means a day on which the Clearing Systems are open for business.

## 8. **PRESCRIPTION**

Claims against the Society in respect of any amounts payable in respect of the CCDS represented by the Global CCDS Certificate will be prescribed after 12 years from the due date and shall revert to the Society.

## 9. **PURCHASE AND CANCELLATION**

Cancellation of any CCDS purchased and surrendered for cancellation in accordance with Condition 8.2 will be effected by a corresponding reduction in the number of CCDS represented by the Global CCDS Certificate.

## 10. **DIRECT RIGHTS**

Subject as follows, upon a breach of contract by the Society (which shall, for the purposes of this paragraph “*Direct Rights*”, include a CCDS holder becoming entitled to bring any action against the Society as contemplated by Condition 11.4) or upon a winding-up or dissolution of the Society, each Beneficial Owner at the time of such breach or, as the case may be, at the Relevant Time (each a **Relevant Person**) shall (for the purpose only of bringing an action for such breach of contract or, as the case may be, claiming in the winding-up or dissolution of the Society in accordance with Condition 4) acquire against the Society all those rights (**Direct Rights**) which such Relevant Person would have had if, at the time of the relevant breach of contract or, as the case may be, at the Relevant Time, such Relevant Person had been identified in the CCDS Register as the registered holder of such number of CCDS (the **Underlying CCDS**) as is equal to the number of CCDS which are credited to such Relevant Person’s securities account with a Clearing System (or, as the case may be, with any Intermediary) at such time.

The Relevant Persons will acquire such Direct Rights only in the circumstances and for the purposes described in the preceding paragraph and for no other purpose. Direct Rights will be acquired automatically at the time of the relevant breach of contract or, as the case may be, at the Relevant Time, without the need for any further action on behalf of any person. The Society’s obligation hereunder shall be a separate and independent obligation to each Relevant Person by reference to each Underlying CCDS of such Relevant Person, and the Society agrees that a Relevant Person may assign such Direct Rights in whole or in part.

The records of the Clearing Systems and (subject to the following proviso) each Intermediary (as applicable) shall be conclusive evidence of the identity of the Relevant Persons and the number of Underlying CCDS credited to the securities account of each Relevant Person; provided that the records of an Intermediary shall be conclusive evidence of the identity of any Relevant Persons only if accompanied by records of (i) the Accountholder (and any other Intermediary) through which such Intermediary holds the relevant CCDS and (ii) the relevant Clearing System, which records when taken together evidence a chain of ownership linking the records of such Intermediary and the records of the relevant Clearing System. For these purposes, a statement issued by a relevant Clearing System and/or a relevant Intermediary (as applicable) stating the name of the Relevant Person to which the statement is issued and the number of Underlying CCDS credited to the securities account of such Relevant Person as at the opening of business on the first business day following the time of the relevant breach of contract or the Relevant Time (as the case may be), shall be conclusive evidence of the records of the relevant Clearing System or (subject to the foregoing proviso) such Intermediary (as the case may be) at the time of the relevant breach of contract or the Relevant Time (as applicable).



## **11. SUCCESSION AND TRANSFERS**

Upon a transfer by the Society of the whole of its business to a Successor Entity in accordance with Condition 10.2, the Nominee will (unless otherwise agreed as part of the terms of the transfer at the relevant time) direct that the ordinary shares to be delivered to it shall instead be delivered directly to (or to the order of) the Beneficial Owners as if those Beneficial Owners had, at the vesting date, held in definitive form the number of CCDS corresponding to their book-entry interest in the CCDS at that time.

## PART X – TERMS AND CONDITIONS OF THE TIER 2 NOTES

*The following (excluding italicised paragraphs) is the text of the terms and conditions that, subject to completion and amendment, shall be applicable to the Tier 2 Notes in definitive form (if any) issued in exchange for the Global Tier 2 Certificate.*

The issue of the £22,498,600 11.00 per cent. Tier 2 Subordinated Notes due 2038 (the **Notes**) of West Bromwich Building Society (the **Society**) was authorised by a resolution of the Board of Directors of the Society passed on 27 February 2018. The Notes are issued subject to and with the benefit of an Agency Agreement dated 12 April 2018 (such agreement as amended and/or supplemented and/or restated from time to time, the **Agency Agreement**) made between the Society, Citibank N.A., London Branch as registrar and transfer agent (the **Registrar** and, together with any other transfer agents appointed under the Agency Agreement from time to time, the **Transfer Agents**) and Citibank N.A., London Branch as fiscal agent and principal paying agent (the **Fiscal Agent** and, together with any other paying agents appointed under the Agency Agreement from time to time, the **Paying Agents**, and the Paying Agents and the Transfer Agents together, the **Agents**). These Conditions include summaries of, and are subject to, the detailed provisions of the Agency Agreement, which is available for inspection during usual business hours at the specified offices of the Registrar and the Fiscal Agent. The holders of the Notes are entitled to the benefit of, are bound by, and are deemed to have notice of those provisions applicable to them of the Agency Agreement. References in these Conditions to the Fiscal Agent, the Registrar, the Paying Agents, the Transfer Agents and the Agents shall include any additional or successor agent appointed in such capacity under the Agency Agreement.

### 1 Transfers of Notes

#### (a) Transfer

A holding of Notes may, subject to Condition 1(d), be transferred in whole or in part upon the surrender (at the specified office of the Registrar or any Transfer Agent) of the Certificate(s) representing such Notes to be transferred, together with the form of transfer endorsed on such Certificate(s) duly completed and executed and any other evidence as the Registrar or Transfer Agent may reasonably require. In the case of a transfer of part only of a holding of Notes represented by one Certificate, a new Certificate shall be issued to the transferee in respect of the part transferred and a further new Certificate in respect of the balance of the holding not transferred shall be issued to the transferor. In the case of a transfer of Notes to a person who is already a holder of Notes, a new Certificate representing the enlarged holding shall only be issued against surrender of the Certificate representing the existing holding. All transfers of Notes and entries in the Register will be made in accordance with the detailed regulations concerning transfers of Notes scheduled to the Agency Agreement. The regulations may be changed by the Society, with the prior written approval of the Registrar. A copy of the current regulations will be made available by the Registrar to any holder upon request.

#### (b) Delivery of New Certificates

Each new Certificate to be issued pursuant to Condition 1(a) shall be available for delivery within three business days of receipt of a duly completed form of transfer and surrender of the existing Certificate(s). Delivery of the new Certificate(s) shall be made at the specified office of the Transfer Agent or of the Registrar (as the case may be) to whom delivery or surrender of such form of transfer or Certificate shall have been made or, at the option of the holder making such delivery or surrender as aforesaid and as specified in the relevant form of transfer or otherwise in writing, be mailed by uninsured post at the risk of the holder entitled to the new Certificate to such address as may be so specified, unless such holder requests otherwise and pays in advance to the relevant Transfer Agent or the Registrar (as the case may be) the costs of such other method of delivery and/or such insurance as it may specify. In this Condition 1(b), **business day** means a day, other

than a Saturday or Sunday, on which banks are open for business in the place of the specified office of the relevant Transfer Agent or the Registrar (as the case may be).

**(c) Transfer Free of Charge**

Certificates, on transfer, shall be issued and registered without charge by or on behalf of the Society, the Registrar or any Transfer Agent, but upon payment of any tax or other governmental charges that may be imposed in relation to such transfer (or the giving of such indemnity as the Registrar or the relevant Transfer Agent may require).

**(d) Closed Periods**

No holder may require the transfer of a Note to be registered (i) during the period of 15 days ending on (and including) the due date for redemption of that Note, (ii) during the period of 15 days prior to (and including) any date on which Notes may be called for redemption by the Society at its option pursuant to Condition 6(c), (iii) after the Notes have been called for redemption, or (iv) during the period of seven days ending on (and including) any Record Date.

**2 Form, Denomination and Title**

**(a) Form and Denomination**

The Notes are serially numbered in the denominations of £1,000 and integral multiples of £100 in excess thereof.

The Notes are represented by registered certificates (**Certificates**) and, save as provided in Condition 1(a), each Certificate shall represent the entire holding of Notes by the same holder.

**(b) Title**

Title to the Notes shall pass by registration in the register that the Society shall procure to be kept by the Registrar in accordance with the provisions of the Agency Agreement (the **Register**). Except as ordered by a court of competent jurisdiction or as required by law, the holder of any Note shall be deemed to be and may be treated as its absolute owner for all purposes whether or not it is overdue and regardless of any notice of ownership, trust or an interest in it, any writing on the Certificate representing it or the theft or loss of such Certificate and no person shall be liable for so treating the holder.

In these Conditions, **holder** means the person in whose name a Note is registered.

**3 Status**

The Notes constitute direct, unsecured and subordinated obligations of the Society and rank *pari passu* and without any preference among themselves. The rights and claims of holders in respect of, or arising under, their Notes (including any damages awarded for breach of obligations in respect thereof) are subordinated as described in Condition 4.

**4 Subordination**

**(a) Subordination of Claims in a Winding-up**

In the event of the winding up or dissolution of the Society (other than an Excluded Dissolution), the claims in respect of principal, interest and any other amount (including, without limitation, any damages awarded for breach of the Society's obligations) in respect of the Notes will:

- (i) be subordinated in right of payment in the manner provided below to (x) all Senior Claims, (y) all Senior Non-Preferred Claims, and (z) those Subordinated Claims (if any) which rank, or are expressed to rank, in priority to claims in respect of the Notes;
- (ii) rank at least *pari passu* with claims in respect of the Society's obligations which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 2 Capital; and
- (iii) rank in priority to claims in respect of obligations of the Society which constitute, or would but for any applicable limitation on the amount of such capital constitute, Additional Tier 1 Capital (including, without limitation, and for so long as any of the same remain outstanding, the Existing PIBS) or CET1 Capital (including, for so long as any of the same remain outstanding, the CCDS) and in priority to any other claims ranking, or expressed to rank, junior to the claims in respect of Notes.

Accordingly, if the Society is at any time in a winding-up or dissolution (other than an Excluded Dissolution), then no principal, interest or other amounts (including any damages awarded for breach of the Society's obligations) in respect of the Notes (whether or not already due or accrued prior to the commencement of such winding-up or dissolution) shall be payable by, nor shall any claim in respect thereof be provable against, the Society in such winding-up or dissolution unless and until, and except to the extent that, the Society could make such payment in whole or in part and still be solvent immediately thereafter.

For these purposes, the Society shall be deemed to be **solvent** if it is able to pay its Senior Claims, Senior Non-Preferred Claims and more senior-ranking Subordinated Claims (if any) in full, or the liquidator or other insolvency official of the Society determines that it will be able to do so within a period not exceeding twelve months, and in determining whether the Society is deemed to be solvent for these purposes there shall be disregarded obligations which are not provable in the winding-up or dissolution.

**(b) Waiver of Set-off**

Subject to applicable law, no holder of Notes may exercise, claim or plead any right of set-off, compensation or retention in respect of any amount owed to it by the Society arising under or in connection with the Notes and each holder shall, by virtue of being the holder of any such Note, be deemed to have waived all such rights of set-off, compensation or retention.

Notwithstanding the provision of the foregoing sentence, if any of the said rights and claims of any holder of Notes against the Society is discharged by set-off, such holder of Notes will immediately pay an amount equal to the amount of such discharge to the Society or, in the event of the winding up or dissolution of the Society, the liquidator or other insolvency official of the Society and accordingly such discharge will be deemed not to have taken place.

**(c) Senior Creditors Hierarchy Law**

If, at any time (the **Effective Time**), any law or regulation (a **Senior Creditors Hierarchy Law**) becomes effective which amends the United Kingdom insolvency laws or rules as they apply to the Society (including, without limitation, any law or regulation implementing the amendments to Article 108 of Directive 2014/59/EU made pursuant to Directive (EU) 2017/2399) to provide that, in normal insolvency proceedings, ordinary senior unsecured claims which are not otherwise preferred by law (**Statutory Ordinary Unsecured Claims**) shall nevertheless have a higher priority ranking than other unsecured claims resulting from a debt instrument which meets certain specified conditions (which may, but need not, include a requirement that such debt instrument (i) has an original contractual maturity of at least one year, (ii) contains no embedded derivatives and is not a derivative itself and/or (iii) is issued under terms and/or other documentation which explicitly refers

to such lower ranking) (**Statutory Lower-Ranking Senior Unsecured Claims**), then the Society and, by virtue of its holding of any Note or any beneficial interest therein, each holder or beneficial owner of Notes acknowledges and agrees that (unless the relevant insolvency laws or rules provide otherwise), in the event of a winding up or dissolution of the Society (other than an Excluded Dissolution) which occurs at or after the Effective Time, claims in respect of the Notes will be subordinate to Statutory Lower-Ranking Senior Unsecured Claims.

## **5 Interest**

### **(a) Interest Rate**

The Notes bear interest on their outstanding principal amount at a fixed rate of 11.00 per cent. per annum (the **Interest Rate**) from (and including) the Issue Date in accordance with the provisions of this Condition 5.

### **(b) Interest Payment Dates**

Interest shall be payable on the Notes semi-annually in arrear in equal instalments on 12 April and 12 October in each year, from (and including) 12 October 2018 up to (and including) the Maturity Date (each an **Interest Payment Date**) as provided in this Condition 5.

### **(c) Calculation of Interest**

Interest will be payable in arrear on each Interest Payment Date in respect of the Interest Period ending immediately prior to such Interest Payment Date.

Interest in respect of any Note for any period which is not a full Interest Period shall be calculated per Calculation Amount. The amount of interest per Calculation Amount shall be equal to the product of (i) the Calculation Amount, (ii) the Interest Rate and (iii) the day-count fraction as described in the following paragraph for the relevant period, rounding the resultant figure to the nearest penny (half a penny being rounded upwards). The amount of interest payable in respect of a Note is the aggregate of the amounts (calculated as aforesaid) for each Calculation Amount comprising the denomination of the Note.

Where it is necessary to compute an amount of interest in respect of any Note for a period which is less than a full Interest Period, the relevant day-count fraction shall be determined on the basis of (A) the number of days in the relevant period, from (and including) the date from which interest begins to accrue to (but excluding) the date on which it falls due, divided by (B) the product of (x) two and (y) the actual number of days in the Interest Period in which the relevant period falls.

### **(d) Interest Amounts**

The amount of interest payable in respect of each Calculation Amount on each Interest Payment Date shall be £5.50. The amount of interest payable in respect of each Note, is the aggregate of the amounts for each Calculation Amount comprising the denomination of the Note.

### **(e) Interest Accrual**

The Notes will cease to bear interest from (and including) the due date for redemption thereof pursuant to Condition 6(a), 6(c), 6(d) or 6(e), as the case may be, unless, upon surrender of the Certificate representing any Note, payment of all amounts due in respect of such Note is not properly and duly made, in which event interest shall continue to accrue on the Notes at the Interest Rate, both before and after judgment, and shall be payable, as provided in these Conditions up to (but excluding) the Relevant Date.

**(f) Determinations of Fiscal Agent**

All notifications, opinions, determinations, certificates, calculations and decisions given, expressed, made or obtained for the purposes of these Conditions by the Fiscal Agent, shall (in the absence of manifest error) be binding on the Society, the Transfer Agents, the Paying Agents and all holders and (in the absence of wilful default or fraud) no liability to the holders or the Society shall attach to the Fiscal Agent in connection with the exercise or non-exercise by it of any of its powers or duties hereunder.

**6 Redemption and Purchase**

**(a) Final Redemption**

Unless previously redeemed or purchased and cancelled, the Notes will be redeemed at their principal amount, together with accrued and unpaid interest, on 12 April 2038 (the **Maturity Date**). The Notes may not be redeemed other than in accordance with this Condition 6.

**(b) Conditions to Redemption and Purchase**

Any redemption or purchase of the Notes in accordance with Conditions 6(c), 6(d), 6(e) or 6(f) is subject to:

- (i) the Society obtaining prior Supervisory Permission therefor;
- (ii) either:
  - (A) the Society having replaced the Notes with own funds instruments of equal or higher quality at terms that are sustainable for the income capacity of the Society; or
  - (B) the Society having demonstrated to the satisfaction of the Supervisory Authority that the own funds of the Society would, following such redemption or purchase, exceed its minimum capital requirements (including any capital buffer requirements) by a margin that the Supervisory Authority considers necessary at such time; and
- (iii) in the case of any redemption prior to the fifth anniversary of the Issue Date:
  - (A) in the case of redemption upon a Tax Event, the Society having demonstrated to the satisfaction of the Supervisory Authority that the change in tax treatment is material and was not reasonably foreseeable as at the Issue Date; or
  - (B) in the case of redemption upon the occurrence of a Capital Disqualification Event, the Society having demonstrated to the satisfaction of the Supervisory Authority that the relevant change in the regulatory classification of the Notes was not reasonably foreseeable as at the Issue Date.

Notwithstanding the above conditions, if, at the time of any redemption or purchase, the prevailing Regulatory Capital Requirements permit the repayment or purchase only after compliance with one or more alternative or additional pre-conditions to those set out above in this Condition 6(b), the Society shall comply with such additional and/or alternative pre-condition(s) in addition to or, as the case may be, in the alternative to the foregoing.

**(c) Society's Call Option**

Subject to Condition 6(b), the Society may, by giving not less than 30 nor more than 60 days' notice to the holders (in accordance with Condition 13), the Registrar and the Fiscal Agent (which notice shall be irrevocable), elect to redeem all, but not some only, of the Notes on the First Call Date or

any Interest Payment Date thereafter at their principal amount, together with any unpaid interest accrued to (but excluding) the date fixed for redemption. Upon the expiry of such notice, the Society shall redeem the Notes.

**(d) Redemption following a Tax Event**

If, prior to the giving of the notice referred to in this Condition 6(d), a Tax Event has occurred, then the Society may, subject to Condition 6(b) and having given not less than 30 nor more than 60 days' notice to the holders (in accordance with Condition 13), the Registrar and the Fiscal Agent (which notice shall be irrevocable and shall specify the date for redemption), elect to redeem in accordance with these Conditions at any time all, but not some only, of the Notes at their principal amount, together with any unpaid interest accrued to (but excluding) the date fixed for redemption. Upon the expiry of such notice, the Society shall redeem the Notes.

**(e) Redemption following a Capital Disqualification Event**

If, prior to the giving of the notice referred to in this Condition 6(e), a Capital Disqualification Event has occurred, then the Society may, subject to Condition 6(b) and having given not less than 30 nor more than 60 days' notice to the holders (in accordance with Condition 13), the Registrar and the Fiscal Agent (which notice shall be irrevocable and shall specify the date for redemption), elect to redeem in accordance with these Conditions at any time all, but not some only, of the Notes at their principal amount, together with any unpaid interest accrued to (but excluding) the date fixed for redemption. Upon the expiry of such notice, the Society shall redeem the Notes.

**(f) Purchases**

The Society and its subsidiaries may, subject to Condition 6(b) and to compliance with prevailing Regulatory Capital Requirements, at any time purchase (or otherwise acquire), or procure others to purchase (or otherwise acquire) beneficially for its account, Notes in any manner and at any price. All Notes so purchased may, at the option of the Society, be held, reissued, resold or surrendered to the Registrar for cancellation.

**(g) Cancellation**

All Notes redeemed pursuant to this Condition 6, and all Notes purchased by the Society or its subsidiaries and surrendered to the Registrar for cancellation, will forthwith be cancelled. Any Notes so cancelled may not be reissued or resold and the obligations of the Society in respect of any such Notes shall be discharged.

## **7 Payments**

**(a) Method of Payment**

- (i) Payments of principal shall be made (subject to surrender of the relevant Certificates at the specified office of any Transfer Agent or of the Registrar if no further payment falls to be made in respect of the Notes represented by such Certificates) in like manner as provided for payments of interest in paragraph (ii) below.
- (ii) Interest on each Note shall be paid to the person shown in the Register at the close of business on the fifteenth day before the due date for payment thereof (the **Record Date**). Payments of interest on each Note shall be made in pounds sterling by transfer to a pounds sterling account maintained by the payee with a bank in London.

**(b) Payments Subject to Laws**

Payments in respect of the Notes will be subject in all cases to (i) any fiscal or other laws and regulations applicable thereto in the place of payment, but without prejudice to the provisions of Condition 9, and (ii) any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the U.S. Internal Revenue Code of 1986 (the **Code**) or otherwise imposed pursuant to Sections 1471 through 1474 of the Code, any regulations or agreements thereunder, any official interpretations thereof, or any law implementing an intergovernmental approach thereto.

**(c) Payments on Business Days**

Payment is to be made by transfer to an account in pounds sterling, and payment instructions (for value the due date, or if that date is not a Business Day, for value the first following day which is a Business Day) will be initiated on the last day on which the Fiscal Agent is open for business preceding the due date for payment or, in the case of payments of principal where the relevant Certificate has not been surrendered at the specified office of any Transfer Agent or of the Registrar, on a day on which the Fiscal Agent is open for business and on which the relevant Certificate is surrendered.

**(d) Delay in Payment**

Holders will not be entitled to any interest or other payment for any delay after the due date in receiving the amount due on a Note if the due date is not a Business Day or if the holder is late in surrendering or cannot surrender its Certificate (if required to do so).

**8 Enforcement**

**(a) Non-payment when due**

If default is made for a period of seven days or more in the payment of any principal due on the Notes or any of them or for a period of 14 days or more in the payment of any interest due on the Notes or any of them and such default is continuing, the holder of any Note may institute proceedings for the winding up of the Society in England (but not elsewhere) to enforce the obligations of the Society in respect of such holder's Notes, but may take no other action in respect of such default (except as provided in Condition 8(b)).

**(b) Winding-up or dissolution**

In the event of a winding-up or dissolution of the Society (other than an Excluded Dissolution), whether or not instituted by a holder pursuant to Condition 8(a), the holder of any Note may give notice to the Society (or the relevant official presiding over such winding-up or dissolution) that such holder's Notes are, and such Notes shall accordingly immediately become, due and repayable at their principal amount together with accrued and unpaid interest, and such holder shall be entitled to claim and/or prove in such winding-up or dissolution in respect of such Notes (such claim being subordinated as provided in Condition 4).

**(c) Other limited rights of enforcement**

Without prejudice to Conditions 8(a) and 8(b), a holder may institute such steps, actions or proceedings against the Society as it may think fit to enforce any term or condition binding on the Society under the Notes (other than any payment obligation of the Society under or arising from the Notes, including, without limitation, payment of any principal, interest or other amounts in respect of the Notes or any damages awarded for breach of any obligations); provided, however, that in no event shall the Society, by virtue of the institution of any such steps, actions or proceedings, be obliged to pay any sum or sums, in cash or otherwise, sooner than the same would otherwise have



been payable by it pursuant to these Conditions, nor will any holder accept the same, otherwise than during or after a winding-up or dissolution of the Society.

**(d) Extent of remedy**

No remedy against the Society, other than the institution of proceedings for the winding up in England of the Society as provided in Condition 8(a) and/or the proving or claiming in any winding-up or dissolution of the Society as provided in Condition 8(b), shall be available to the holders for the recovery of amounts owing in respect of the Notes. Furthermore, no holder may institute proceedings for the winding up of the Society to enforce the obligations of the Society in respect of the Notes, except in the circumstances provided in Condition 8(a).

**9 Taxation**

**(a) Withholding and Additional Amounts**

All payments of principal, interest and any other amounts by or on behalf of the Society in respect of the Notes shall be made free and clear of, and without withholding or deduction for or on account of, any present or future taxes, duties, assessments or governmental charges of whatever nature imposed, levied, collected, withheld or assessed by the United Kingdom, unless such withholding or deduction is required by law. In that event the Society will, in respect of payments of interest only (but not in respect of payments of principal), pay such additional amounts (**Additional Amounts**) as may be necessary in order that the net amount of interest received by the holders after such withholding or deduction shall equal the amount of interest which would have been receivable by them in the absence of such withholding or deduction; except that no such Additional Amounts shall be payable in respect of any Note:

- (i) held by or on behalf of a holder who is subject to such taxes, duties, assessments or governmental charges in respect of such Note by reason of having some connection with the United Kingdom otherwise than merely by holding the Note or by the receipt of amounts in respect of the Note; or
- (ii) held by or on behalf of a holder who would not be liable or subject to the withholding or deduction by making a declaration of non-residence or other similar claim for exemption to the relevant tax authority; or
- (iii) in respect of which the certificate representing such Note is presented for payment more than 30 days after the Relevant Date, except to the extent that the holder would have been entitled to such Additional Amounts on presenting the Note for payment on the last day of such period of 30 days.

Notwithstanding any other provision of these Conditions, in no event will Additional Amounts be payable by (or on behalf of) the Society under this Condition 9 or otherwise in respect of any withholding or deduction required pursuant to an agreement described in Section 1471(b) of the Code or otherwise imposed pursuant to Sections 1471 through 1474 of the Code (or any regulations or agreements thereunder or any official interpretations thereof) or an intergovernmental agreement between the United States and another jurisdiction facilitating the implementation thereof or any law implementing such an intergovernmental agreement.

**(b) Interpretation of interest**

References in these Conditions to any amount of interest payable in respect of the Notes shall be deemed also to refer to any Additional Amounts which may be payable under this Condition 9.

## **10 Prescription**

Claims against the Society for payment in respect of the Notes shall be prescribed and become void unless made within 10 years (in the case of principal) or five years (in the case of interest) from the appropriate Relevant Date in respect of them.

## **11 Meetings of holders, Modification, Waiver and Substitution**

### **(a) Supervisory Permission**

No modification to these Conditions or substitution of the Society shall become effective unless the Society shall have received Supervisory Permission therefor (unless Supervisory Permission is not then required for such modification or substitution pursuant to the Regulatory Capital Requirements).

### **(b) Meetings of holders**

The Agency Agreement contains provisions for convening meetings of holders to consider any matter affecting their interests, including the sanctioning by Extraordinary Resolution of a modification of any of these Conditions or any provisions of the Agency Agreement. Such a meeting may be convened by the Society or by holders holding not less than 10 per cent. in principal amount of the Notes for the time being outstanding.

The quorum at any such meeting for passing an Extraordinary Resolution will be one or more persons holding or representing a clear majority in principal amount of the Notes for the time being outstanding, or at any adjourned meeting one or more persons being or representing holders whatever the principal amount of the Notes so held or represented, except that at any meeting the business of which includes the modification of certain of these Conditions (including, *inter alia*, the provisions regarding subordination referred to in Condition 4, the terms concerning currency and due dates for payment of principal or interest payments in respect of the Notes and reducing or cancelling the principal amount of, or interest on, any Notes or the Interest Rate) the quorum will be one or more persons holding or representing not less than two-thirds, or at any adjourned such meeting not less than one-third, in principal amount of the Notes for the time being outstanding.

An Extraordinary Resolution passed at any meeting of holders will be binding on all holders, whether or not they are present at the meeting and whether or not voting in favour.

The Agency Agreement provides that (i) a resolution passed, at a meeting duly convened and held, by a majority of at least 75 per cent. of the votes cast, (ii) a resolution in writing signed by or on behalf of the holders of not less than 75 per cent. in principal amount of the Notes for the time being outstanding or (iii) consent given by way of electronic consents through the relevant clearing system(s) by or on behalf of the holder(s) of not less than 75 per cent. in principal amount of the Notes for the time being outstanding, shall, in each case, be effective as an Extraordinary Resolution of the holders.

Any resolution approved by holders of the requisite principal amount of Notes referred to above will be binding on all holders, whether or not participating in the relevant vote and (if participating) whether or not voting in favour.

**(c) Modification and Waiver**

The Fiscal Agent and the Society may agree, without the consent of the holders, to:

- (i) any modification of these Conditions or of any other provisions of the Agency Agreement which, in the opinion of the Society, is of a formal, minor or technical nature or is made to correct a manifest error or to comply with mandatory provisions of the law; or
- (ii) any other modification to, and any waiver or authorisation of any breach or proposed breach of, any of these Conditions or of the provisions of the Agency Agreement which, in the opinion of the Society, is not materially prejudicial to the interests of the holders.

**(d) Substitution**

*(i) Conditions Precedent to Substitution*

The Society may, without the consent of the holders, be replaced and substituted by any other entity as principal debtor (the **Substitute Obligor**) in respect of the Notes provided that:

- (A) a deed poll and/or any other document(s) shall be executed by the Substitute Obligor as may be necessary to give full effect to the substitution (together the **Documents**) and (without limiting the generality of the foregoing) pursuant to which the Substitute Obligor shall undertake in favour of each holder to be bound by the Conditions of the Notes and the provisions of the Agency Agreement as fully as if the Substitute Obligor had been named in the Notes and the Agency Agreement as the principal debtor in respect of the Notes in place of the Society (or any previous substitute) and pursuant to which the Society shall irrevocably and unconditionally guarantee, on a subordinated basis equivalent to the subordination set out in Condition 4, in favour of each holder the payment of all sums payable by the Substitute Obligor as such principal debtor;
- (B) without prejudice to the generality of paragraph (A) above, where the Substitute Obligor is incorporated, domiciled or resident for taxation purposes in a territory other than the United Kingdom, the Documents shall contain a covenant by the Substitute Obligor and/or such other provisions as may be necessary to ensure that each holder has the benefit of a covenant in terms corresponding to the provisions of Condition 9 with the substitution for the references to the United Kingdom of references to the territory or territories in which the Substitute Obligor is incorporated, domiciled and/or resident for taxation purposes;
- (C) any stock exchange on which the Notes are listed shall have confirmed that following the proposed substitution of the Substitute Obligor the Notes will continue to be listed on such stock exchange; and
- (D) (if the Substitute Obligor is incorporated in a jurisdiction other than England and Wales) the Substitute Obligor shall have appointed an agent for service of process in England to receive service of process on its behalf in relation to any legal action or proceedings arising out of or in connection with the Notes.

*(ii) Assumption by Substitute Obligor*

Upon execution of the Documents as referred to in Condition 11(d)(i) above, the Substitute Obligor shall be deemed to be named in the Notes as the principal debtor in place of the Society (or of any previous substitute under these provisions) and the Notes shall thereupon be deemed to be amended to give effect to the substitution. The execution of the Documents shall operate to release the Society (or such previous substitute as aforesaid) from all of its obligations as issuer in respect of

the Notes (but this shall be without prejudice to its obligations as guarantor as provided in Condition 11(d)(i)).

*(iii) Deposit of Documents*

The Documents shall be deposited with and held by the Fiscal Agent for so long as any Note remains outstanding and for so long as any claim made against the Substitute Obligor or the Society by any holder in relation to the Notes or the Documents shall not have been finally adjudicated, settled or discharged.

**(e) Notices**

Any such modification, waiver, authorisation or substitution shall be binding on all holders and, unless the Fiscal Agent agrees otherwise, any such modification or substitution shall be notified to the holders in accordance with Condition 13 as soon as practicable thereafter.

**12 Replacement of Certificates**

If any Certificate is lost, stolen, mutilated, defaced or destroyed, it may be replaced, subject to applicable laws and regulations, at the specified office of the Registrar, in each case on payment by the claimant of the fees and costs incurred in connection therewith and on such terms as to evidence, security, indemnity and otherwise as the Society or the Registrar may reasonably require. Mutilated or defaced Certificates must be surrendered before replacements will be issued.

**13 Notices**

Notices to the holders shall be mailed to them at their respective addresses in the Register and deemed to have been given on the first weekday (being a day other than a Saturday or Sunday) in London after the date of mailing.

The Society shall also ensure that all notices are duly published (if such publication is required) in a manner which complies with the rules and regulations of any stock exchange on which the Notes are for the time being listed and/or admitted to trading.

**14 Further Issues**

The Society may from time to time, without the consent of the holders but subject to any Supervisory Permission (if any) as may be required, create and issue further securities either (i) having the same terms and conditions as the Notes in all respects (or in all respects except for the first payment of interest on them) and so that such further issue shall be consolidated and form a single series with the outstanding Notes or (ii) upon such terms as the Society may determine at the time of their issue. References in these Conditions to the Notes include (unless the context requires otherwise) any other securities issued pursuant to this Condition and forming a single series with the Notes.

**15 Agents**

The initial Fiscal Agent and Registrar and their initial specified offices are specified in the Agency Agreement. They act solely as agents of the Society and do not assume any obligation or relationship of agency or trust for or with any holder. The Society reserves the right at any time to vary or terminate the appointment of the Fiscal Agent, the Registrar, any Paying Agent and any Transfer Agent and to appoint successor or additional Agents, provided that it will:

- (a) at all times maintain a Fiscal Agent, a Registrar, a Paying Agent and a Transfer Agent (which roles may be comprised in one or more entities); and

- (b) so long as any of the Notes are admitted to listing or trading on any stock exchange (with the consent of the Society), a Paying Agent (which may be the Fiscal Agent or Registrar) having a specified office in each location required by the rules and regulations of the relevant stock exchange.

Notice of any such termination or appointment and of any change in the specified offices of the Agents will be given to the Holders in accordance with Condition 13.

## **16 Governing Law**

The Notes and any non-contractual obligations arising out of or in connection with them are governed by, and shall be construed in accordance with, the laws of England.

## **17 Contracts (Rights of Third Parties) Act 1999**

No person shall have any right to enforce any term or condition of the Notes by virtue of the Contracts (Rights of Third Parties) Act 1999.

## **18 Definitions**

In these Conditions:

**Additional Amounts** has the meaning given to it in Condition 9;

**Additional Tier 1 Capital** has the meaning given to such term (or to any successor or equivalent term) in the Regulatory Capital Requirements;

**Agency Agreement** has the meaning given to it in the preamble to these Conditions;

**Agents** has the meaning given to it in the preamble to these Conditions;

**Business Day** means a day, other than a Saturday, Sunday or public holiday, on which commercial banks and foreign exchange markets are open for general business in London;

**Calculation Amount** means £100 in principal amount of the Notes;

a **Capital Disqualification Event** is deemed to have occurred if there is a change (which has occurred or which the Supervisory Authority considers to be sufficiently certain) in the regulatory classification of the Notes which becomes effective after the Issue Date and that results, or would be likely to result, in the entire principal amount of the Notes or any part thereof being excluded from the Tier 2 Capital of the Society (whether on an individual or consolidated basis);

**CCDS** means Core Capital Deferred Shares (within the meaning given in the Rules of the Society) issued by the Society;

**Certificate** has the meaning given in Condition 2(a);

**CET1 Capital** has the meaning given to such term (or to any successor or equivalent term) in the Regulatory Capital Requirements;

**Conditions** means these terms and conditions of the Notes, as amended from time to time;

**Deferred Shares** has the meaning given in the Rules of the Society;

**Effective Time** has the meaning given in Condition 4(c);

**Excluded Dissolution** means each of:

- (i) a winding-up or dissolution of the Society for the purpose of a reconstruction or amalgamation or the substitution in place of the Society of a successor in business the terms of which have previously been approved by an Extraordinary Resolution of the holders; and
- (ii) a dissolution of the Society by virtue of the amalgamation and transfer provisions set out in sections 93, 94 and 97 of the Building Societies Act 1986, as amended, or by virtue of a transfer pursuant to an order made under section 3 of the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007, as amended (or any successor provisions thereto);

**Existing PIBS** means the Society's 6.15 per cent. Permanent Interest Bearing Shares (originally issued in an aggregate principal amount of £75 million);

**Extraordinary Resolution** has the meaning given in the Agency Agreement;

**First Call Date** means 12 April 2033;

**Fiscal Agent** has the meaning given to it in the preamble to these Conditions;

**holder** has the meaning given to it in Condition 2(b);

**Interest Payment Date** has the meaning given to it in Condition 5(b);

**Interest Period** means the period from (and including) the Issue Date to (but excluding) the first Interest Payment Date and each successive period from (and including) an Interest Payment Date to (but excluding) the next succeeding Interest Payment Date;

**Interest Rate** has the meaning given to it in Condition 5(a);

**Issue Date** means 12 April 2018;

**Maturity Date** has the meaning given to it in Condition 6(a);

**Notes** has the meaning given to it in the preamble to these Conditions;

**Paying Agents** has the meaning given to it in the preamble to these Conditions;

**pounds sterling, pence and £** refer to the lawful currency of the United Kingdom;

**Record Date** has the meaning given to it in Condition 7(a)(ii);

**Register** has the meaning given to it in Condition 2(b);

**Registrar** has the meaning given to it in the preamble to these Conditions;

**Regulatory Capital Requirements** means, at any time, any requirement or provision contained in the law, regulations, requirements, guidelines and policies then in effect relating to capital adequacy and/or prudential supervision and applicable to the Society, including (without limitation to the generality of the foregoing), those laws, regulations, requirements, guidelines and policies relating to capital adequacy and prudential supervision then in effect of the United Kingdom or the Supervisory Authority and/or any regulation, directive or other binding rules, standards or decisions adopted by the institutions of the European Union;

**Relevant Date** means:

- (i) in respect of any payment other than a sum to be paid by the Society in a winding-up or dissolution (other than an Excluded Dissolution) of the Society, the date on which payment in respect of it first becomes due or (if any amount of the money payable is improperly withheld or refused) the date on which payment in full of the amount outstanding is made or (if earlier) the date seven days after that on which notice is duly given to the holders that, upon further surrender of the Certificate representing such Note being made in accordance with the Conditions, such payment will be made, provided that payment is in fact made upon such surrender; and
- (ii) in respect of a sum to be paid by the Society in a winding-up or dissolution (other than an Excluded Dissolution) of the Society, the date which is one day prior to the date on which an order is made or a resolution is passed for the winding-up or, as the case may be, dissolution;

**Rules** means the rules of the Society in force from time to time;

**Senior Claims** means the aggregate amount of all claims admitted in the winding up or dissolution of the Society which are:

- (i) claims of depositors of the Society;
- (ii) claims of Shareholding Members of the Society as regards the principal and interest due on their Shares, other than Deferred Shares; and
- (iii) claims of creditors in respect of unsubordinated obligations of the Society (excluding Senior Non-Preferred Claims);

**Senior Creditors Hierarchy Law** has the meaning given in Condition 4(c);

**Senior Non-Preferred Claims** means the aggregate amount of all claims admitted in the winding-up or dissolution of the Society which are claims of creditors in respect of obligations which rank or are expressed to rank junior to (or have or are expressed to have a lower priority ranking compared to) claims in respect of all Senior Claims of the Society, other than Subordinated Claims;

**Shareholding Member** has the meaning given in the Rules of the Society;

**Shares** has the meaning given in the Rules of the Society;

**Society** has the meaning given to it in the preamble to these Conditions;

**Statutory Lower-Ranking Senior Unsecured Claims** has the meaning given in Condition 4(c);

**Statutory Ordinary Unsecured Claims** has the meaning given in Condition 4(c);

**Subordinated Claims** means the aggregate amount of all claims admitted in the winding-up or dissolution of the Society which rank, or are expressed to rank, junior to claims in respect of Senior Non-Preferred Claims, including (without limitation) claims of creditors in respect of obligations of the Society which constitute, or would but for any applicable limitation on the amount of such capital constitute, Tier 2 Capital, Additional Tier 1 Capital or CET1 Capital;

**Substitute Obligor** has the meaning given to it in Condition 11(d);

**Supervisory Authority** means the Prudential Regulation Authority or such successor or other authority having primary supervisory authority with respect to prudential matters concerning the Society;

**Supervisory Permission** means, in relation to any action, such permission, approval, waiver or, as the case may be, non-objection (if any) from the Supervisory Authority as is required therefor under prevailing Regulatory Capital Requirements at the relevant time;

a **Tax Event** will be deemed to have occurred if, as a result of a Tax Law Change:

- (i) in making any payments on the Notes, the Society has paid or will or would on the next due date for any payment in respect of the Notes be required to pay any Additional Amounts;
- (ii) the Society is no longer, or will no longer be, entitled to claim a deduction in respect of any payments in respect of the Notes in computing its taxation liabilities or the amount of such deduction is or will be reduced;
- (iii) the Notes are, or will be, prevented from being treated as loan relationships for United Kingdom tax purposes; or
- (iv) the Society is not, or will not be, able to have losses or deductions set against any profits or gains, or profits or gains offset by any losses or deductions, of companies with which it is or would otherwise be so grouped for applicable United Kingdom tax purposes (whether under the group relief system current as at the Issue Date or any similar system or systems having like effect as may from time to time exist),

and, in any such case, the Society cannot avoid the foregoing by taking reasonable measures available to it;

**Tax Law Change** means any change in, or amendment to, the laws or regulations of the United Kingdom (including any treaty to which it is a party) or any political subdivision or any authority thereof or therein having power to tax, or any change in the official interpretation thereof by the relevant tax authority or in the application of such laws or regulations by a decision of any court or tribunal that provides for a position with respect to such laws or regulations that differs from the previously generally accepted position in relation to similar transactions or any pronouncement of a tax authority in the United Kingdom, which change or amendment becomes effective or, in the case of a change in law, if such change is enacted by a UK Act of Parliament or by Statutory Instrument, after the Issue Date;

**Tier 2 Capital** has the meaning given to such term (or to any successor or equivalent term) in the Regulatory Capital Requirements;

**Transfer Agents** has the meaning given to it in the preamble to these Conditions; and

**United Kingdom** or **UK** means the United Kingdom of Great Britain and Northern Ireland.



## **SUMMARY OF PROVISIONS RELATING TO THE TIER 2 NOTES WHILE REPRESENTED BY THE GLOBAL TIER 2 CERTIFICATE**

The following is a summary of the provisions to be contained in the Agency Agreement and/or in the Global Tier 2 Certificate (as defined below) which will apply to, and in some cases modify the effect of, the Tier 2 Conditions while the Notes are represented by the Global Tier 2 Certificate:

### **Initial issue of Global Certificate**

The Notes will, upon issue, be represented initially by a single global certificate (the **Global Tier 2 Certificate**), which will be registered in the name of a nominee (the **Registered Holder**) for a common depositary (the **Common Depositary**) for Euroclear Bank SA/NV (**Euroclear**) and Clearstream Banking S.A. (**Clearstream, Luxembourg**) and may be delivered on or prior to the original issue date of the Notes.

Upon the registration of the Global Tier 2 Certificate in the name of any nominee for Euroclear and Clearstream, Luxembourg and delivery of the Global Tier 2 Certificate to the Common Depositary, Euroclear or Clearstream, Luxembourg will credit each subscriber with a principal amount of Notes equal to the principal amount thereof for which it has subscribed and paid.

### **Relationship of Accountholders with Clearing Systems**

Each of the persons (each an **Accountholder**) shown in the records of Euroclear, Clearstream, Luxembourg or any other clearing system (an **Alternative Clearing System**) as the holder of a Note represented by a Global Tier 2 Certificate must look solely to Euroclear, Clearstream, Luxembourg or such Alternative Clearing System (as the case may be) for his share of each payment made by the Society to the registered holder of the Global Tier 2 Certificate and in relation to all other rights arising under the Global Tier 2 Certificate, subject to and in accordance with the respective rules and procedures of Euroclear, Clearstream, Luxembourg or such Alternative Clearing System (as the case may be).

Such persons shall have no claim directly against the Society in respect of payments due on the Note for so long as the Notes are represented by the Global Tier 2 Certificate, and such obligations of the Society will be discharged by payment to the Registered Holder of the Global Tier 2 Certificate in respect of each amount so paid.

### **Exchange of the Global Tier 2 Certificate**

The Global Tier 2 Certificate will be exchangeable (free of charge to the holder) in whole but not in part for Certificates only upon the occurrence of an Exchange Event. An **Exchange Event** means that the Society has been notified that both Euroclear or Clearstream, Luxembourg have been closed for business for a continuous period of 14 days (other than by reason of holiday, statutory or otherwise) or have announced an intention permanently to cease business or have in fact done so and no successor clearing system is available.

The Society will promptly give notice to the holders in accordance with Condition 13 if an Exchange Event occurs. In the event of the occurrence of an Exchange Event, Euroclear and/or Clearstream, Luxembourg, as the case may be, acting on the instructions of any Accountholder may give notice to the Registrar requesting exchange and the Society may also give notice to the Registrar requesting exchange. Any exchange shall occur no later than 30 days after the date of receipt of the first relevant notice by the Registrar.

Exchanges will be made upon presentation of the Global Tier 2 Certificate at the office of the Registrar by or on behalf of the Registered Holder on any day on which banks are open for general business in the jurisdiction of the Registrar and will be effected by the Registrar (a) entering each Accountholder in the Register as the registered holder of the principal amount of Notes equal to such Accountholder's holding of Notes and (b) completing, authenticating and dispatching to each Accountholder a Certificate evidencing such holding. The aggregate principal amount of the Notes evidenced by definitive Certificates issued upon an exchange of the

Global Tier 2 Certificate will be equal to the aggregate outstanding principal amount of the Notes evidenced by the Global Tier 2 Certificate.

### **Direct Rights**

In the event that:

- (i) the Notes as evidenced by the Global Tier 2 Certificate (or any part of it) have become due and repayable in accordance with the Conditions or that the Maturity Date of the Notes has occurred and, in either case, payment in full of the amount due has not been made to the Registered Holder; or
- (ii) following an Exchange Event, the Global Tier 2 Certificate is not duly exchanged for definitive Certificates by the day provided in the Global Tier 2 Certificate,

then from 8.00 p.m. (London time) on such day each Accountholder will become entitled to proceed directly against the Society on, and subject to, the terms of the Global Tier 2 Certificate, and the Registered Holder will have no further rights under the Global Tier 2 Certificate (but without prejudice to the rights any Accountholder may have under this provision).

### **Calculation of Interest**

For so long as all of the Notes are represented by the Global Tier 2 Certificate and such Global Tier 2 Certificate is held on behalf of Euroclear and Clearstream, Luxembourg, interest shall be calculated on the basis of the aggregate principal amount of the Notes represented by the Global Tier 2 Certificate, and not per Calculation Amount as provided in Condition 5.

### **Payments**

All payments in respect of Notes represented by a Global Tier 2 Certificate will be made to, or to the order of, the person whose name is entered on the Register at the close of business on Record Date, provided that for these purposes the Record Date shall be construed as if the reference in Condition 7(a)(ii) to “fifteenth day” were replaced with a reference to “Clearing System Business Day”. **Clearing System Business Day** means Monday to Friday inclusive, except 25 December and 1 January.

### **Notices**

For so long as the Notes are represented by the Global Tier 2 Certificate and such Global Tier 2 Certificate is held on behalf of Euroclear and Clearstream, Luxembourg, notices may be given to the holders by delivery of the relevant notice to Euroclear and/or Clearstream, Luxembourg (as the case may be) for communication to their respective Accountholders in substitution for publication as required by the Tier 2 Conditions. Any such notice shall be deemed to have been given on the date on which the notice is delivered to Euroclear and Clearstream, Luxembourg.

For so long as the Notes are listed on any stock exchange, notices will also be given in accordance with any applicable requirements of such stock exchange.

### **Prescription**

Claims against the Society in respect of any amounts payable in respect of the Notes represented by the Global Tier 2 Certificate will be prescribed after 10 years (in the case of principal) and five years (in the case of interest) from the due date.

## Meetings

For the purposes of any meeting of the holders, the holder of the Notes represented by the Global Tier 2 Certificate shall be treated as being entitled to one vote in respect of each £1.00 in principal amount of the Notes so held.

## Written Resolution and Electronic Consent

For so long as the Notes are in the form of a Global Tier 2 Certificate registered in the name of any nominee for one or more of Euroclear and Clearstream, Luxembourg or another clearing system, then, in respect of any resolution proposed by the Society:

- (i) where the terms of the proposed resolution have been notified to the holder through the relevant clearing system(s), each of the Society and the Fiscal Agent shall be entitled to rely upon approval of such resolution given by way of electronic consents communicated through the electronic communications systems of the relevant clearing system(s) in accordance with their operating rules and procedures by or on behalf of the holders of not less than 75 per cent. in principal amount of the Notes outstanding (**Electronic Consent**). Neither the Society nor the Fiscal Agent shall be liable or responsible to anyone for such reliance; and
- (ii) where Electronic Consent is not being sought, for the purpose of determining whether a written resolution has been validly passed, the Society and the Fiscal Agent shall be entitled to rely on consent or instructions given in writing directly to the Society and/or the Fiscal Agent:
  - (a) by Accountholders in the clearing system(s) with entitlements to such Global Tier 2 Certificate; and/or
  - (b) where the Accountholders hold any such entitlement on behalf of another person, on written consent from or written instruction by the person identified by that accountholder as the person for whom such entitlement is held.

For the purpose of establishing the entitlement to give any such consent or instruction, the Society and the Fiscal Agent shall be entitled to rely on any certificate or other document issued by, in the case of (a) above, Euroclear, Clearstream, Luxembourg or any other relevant Alternative Clearing System and, in the case of (b) above, the relevant clearing system and the Accountholder identified by the relevant clearing system for the purposes of (b) above.

Any resolution passed in such manner shall be binding on all holders, even if the relevant consent or instruction proves to be defective. Any such certificate or other document shall, in the absence of manifest error, be conclusive and binding for all purposes. Any such certificate or other document may comprise any form of statement or print out of electronic records provided by the relevant clearing system (including Euroclear's EUCLID or Clearstream, Luxembourg's Creation Online system) in accordance with its usual procedures and in which the Accountholder of a particular principal or nominal amount of the Notes is clearly identified together with the amount of such holding. Neither the Society nor the Fiscal Agent shall be liable to any person by reason of having accepted as valid or not having rejected any certificate or other document to such effect purporting to be issued by any such person and subsequently found to be forged or not authentic.

## Euroclear and Clearstream, Luxembourg

References in the Global Tier 2 Certificate and this summary to Euroclear and Clearstream, Luxembourg shall be deemed to include references to any Alternative Clearing System approved for the purposes of the Notes by the Society following consultation with the Fiscal Agent and the Registrar.

## PART XI - INDUSTRY OVERVIEW

### 1. ECONOMIC OVERVIEW AND GENERAL TRENDS IN THE UK FINANCIAL SERVICES INDUSTRY

During 2017, the UK economy grew by 1.5 per cent. compared with the same period of the previous year - slightly below the 1.8 per cent. average annual rate of growth recorded in 2016 as a whole, and modestly below the 2.3 per cent. average annual growth rate recorded in 2015.

The UK unemployment rate declined from 5.1 per cent. in the three months to December 2015 to 4.8 per cent. in the three months to December 2016 and to 4.3 per cent. in the three months to November 2017. Consumer price inflation (measured by the percentage change in the consumer price index over 12 months) has been increasing in recent years and was 1.6 per cent. in December 2016 and 3.0 per cent. in December 2017, with the increase driven to a large extent by the depreciation of sterling following the UK's EU-exit referendum in the summer of 2016. The Bank of England's Monetary Policy Committee (MPC) maintained interest rates at 0.5 per cent. from 2009 to mid-2016 and reduced them to 0.25 per cent. in August 2016. The MPC raised interest rates back to 0.5 per cent. in November 2017. Total asset purchases on a cumulative basis under quantitative easing were £427.8 billion in December 2016 and £445 billion on 31 December 2017. According to Nationwide's House Price Index, UK house prices increased by 4.4 per cent. over the 12-month period to December 2015, by 4.5 per cent. over the 12-month period to December 2016, and by 2.7 per cent. over the 12-month period to December 2017. All statistics in this paragraph have been obtained from the sources stated in the notes to the table below.

The table below sets out certain economic indicators for the UK for the periods shown.

	2017	2016	2015	2014	2013
GDP Annual growth rate <sup>(1)</sup> .....	1.5%	1.8%	2.3%	3.1%	2.1%
Bank of England Bank Rate ( <i>per cent.</i> ) <sup>(2)</sup> .....	0.50%	0.25%	0.50%	0.50%	0.50%
Bank of England total asset purchases (£ <i>billions</i> ) <sup>(3)</sup> .....	445.0	427.8	374.9	374.9	375.0
Consumer prices index inflation ( <i>per cent.</i> ) <sup>(4)</sup> .....	3.0%	1.6%	0.2%	0.5%	2.0%
Unemployment rate ( <i>per cent.</i> ) <sup>(5)</sup> .....	4.3%	4.8%	5.1%	5.7%	7.2%
Nationwide House Price Index <sup>(6)</sup> .....	2.6%	4.5%	4.5%	7.2%	8.4%

Notes:

- (1) Data for the fourth quarter of each year (on a year on year basis), seasonally adjusted. Source: Office for National Statistics (ONS).
- (2) As at 31 December in each of 2017, 2016, 2015, 2014 and 2013. Source: Bank of England.
- (3) Cumulative quantity of assets purchased by the creation of central bank reserves on a settled basis as at 31 December in each of 2017, 2016, 2015, 2014 and 2013. Source: Bank of England.
- (4) Percentage change in the consumer price index over 12 months as at December 2017, 2016, 2015, 2014 and 2013. Source: ONS.
- (5) Summary of National Labour Force Survey data, all persons aged 16 and over, seasonally adjusted. Unemployment rate for three months to November 2017 and three months to December 2016, 2015, 2014 and 2013. Source: ONS.
- (6) Seasonally adjusted index over 12 months as at December 2017, 2016, 2015, 2014 and 2013. Source: Nationwide.

The UK has a large and diverse financial services sector, including banks, building societies, insurance companies, conventional and alternative asset managers, brokers and securities dealers. Many sector participants continue to be affected by the ongoing low interest rate environment, significant regulatory developments (see “Part XX: Supervision and Regulation”) and the impact of new technology on customer behaviour and market structures (see “Risks related to the Society's business” of “Part I: Risk Factors”).

## 2. PARTICIPANTS IN THE UK FINANCIAL SERVICES INDUSTRY

The Society's main competitors have traditionally been providers of personal financial services in the UK. These include other building societies, banks, life insurance companies and mutual insurance companies. In recent years, competitive pressures, consolidation and changes in the regulatory environment have led to building societies, banks and insurance companies in the UK increasingly offering similar products and services. In addition, new providers have emerged as competitors in all areas of the UK personal financial services market. A brief description of the organisations with which the Society competes is set out below.

### 2.1 Building societies

Building societies are owned by, and run for the benefit of, their members (see paragraph entitled "Nature of membership" in paragraph 2.2 of "*Part XX: Supervision and Regulation*"), who are typically a large proportion of a society's mortgage and savings customers. As a result, a number of building societies, including the Society, manage their businesses so as to target a higher quality of service and a superior product offering to their customers, sometimes including more attractive interest rates, rather than focussing specifically on profit maximisation. This distinctive proposition and ethos helps to preserve diversity and competition in the UK financial services market.

Building societies are organised under the provisions of the Act (see "*Part XX: Supervision and Regulation*"). The Act imposes a number of restrictions on the operation of a building society as compared to a bank, including:

- defining the purpose of a building society as "that of making loans which are secured on residential property and funded substantially by its members";
- restricting the ability of building societies to engage in certain wholesale banking activities (for example, acting as a market maker in securities, commodities or currencies, trading in commodities or currencies, entering into certain transactions involving derivatives and limiting the risks for which derivatives hedging may be used);
- specifying certain limitations on the amount of non-mortgage lending that a building society is able to write (a minimum of 75 per cent. of loan assets, excluding liquid assets and fixed assets, must be secured on residential property); and
- limiting the volume of wholesale funding a building society may raise (at least 50 per cent. of funding (calculated in accordance with the Act) is required to be raised from retail depositors).

Over the past 25 years, many building societies have merged with other building societies or, in a number of cases, transferred their businesses to the subsidiary of another mutual organisation or demutualised and transferred their businesses to existing or specially formed banks. As a result, the number of building societies in the UK has fallen from 137 in 1985 to 44 as at 31 December 2017. Within the UK retail banking sector there have also been a number of significant business combinations and this trend was accelerated by the global financial crisis which began in 2007. Building societies today continue to hold an important share of the UK mortgage and savings market.

### 2.2 Banks

During the global financial crisis a number of vulnerabilities within the banking business model were exposed and, as a result, the UK witnessed a number of bank failures, including those of Northern Rock and HBOS plc. The UK banking sector also saw the consolidation of a number of weaker institutions. As a result, there are now five major banks in the UK: Barclays Bank PLC (**Barclays**), HSBC Bank plc (**HSBC**), Lloyds Bank plc (**Lloyds**), The Royal Bank of Scotland (**RBS**) and Santander UK plc (**Santander UK**), which together with Nationwide Building Society represented approximately 72 per cent. of mortgage lending and approximately 65

per cent. of household savings as at 31 December 2016 (according to data produced by the BoE) and are therefore both the key competitors for the Society and its peers.

Due to the losses sustained in the financial crisis as well as increased capital and liquidity requirements under the new Basel III and CRD IV regulatory regime, the larger UK banks have been forced to deleverage, rebuild capital and reduce their reliance on wholesale funding. As well as deleveraging, a number of incumbent banks have been through major cost-cutting exercises, have scaled back their branch network and are continuing to spend significant amounts on improving their IT and operational capability. Additionally, several incumbent banks, such as Lloyds and RBS, continue to streamline their businesses and refocus their operations both geographically and by product.

Two of the major UK banks (RBS and Lloyds) received significant Government support in the form of major capital injections and emergency funding during the financial crisis. The UK Government remains the majority shareholder of RBS. In addition, a number of schemes, including the Credit Guarantee Scheme, the Special Liquidity Scheme, FLS and TFS, intended to support the UK financial institutions sector have been made available at different times since 2008. The UK banks currently face an increasingly rigorous regulatory environment (which also affects building societies) and are under closer public scrutiny following a number of material failures in sales practices, regulatory compliance and operations. In addition, those banks involved in capital markets face more stringent capital requirements versus their peers who are not so involved and the future requirement to “ring-fence” their retail activities.

There is also increasing competition in the UK banking market, with a number of medium-sized banks such as Virgin Money, Clydesdale and TSB, banks such as Metro Bank and Handelsbanken, which emphasise relationship banking and customer service with the branch at their core, specialised banks such as One Savings Bank and Shawbrook, which focus on a specific product range and/or customer segment that may be underserved by the large and medium-sized banks and building societies due to their specialised nature and need for bespoke underwriting processes.

### **2.3 Insurance companies**

The UK insurance industry has traditionally been made up of a large number of mutual insurance organisations and several composite insurers originating a range of products, distributed through building societies, banks, direct sales forces and independent financial advisers. Recent trends include consolidation within the industry, the demutualisation of mutual insurers and the entry of building societies and banks into the market as underwriters as well as distributors. In addition, the growth of internet aggregator sites has made price comparison within the insurance industry more easily available.

### **2.4 Other competitors**

A number of large retailers (such as Tesco, Sainsbury’s, Marks and Spencer and the Post Office) sell financial services to their customers, often through co-operation arrangements with existing banks and insurance companies. The UK financial services market also includes a number of non-bank finance companies such as short-term (or “pay-day”) lenders, online specialists, peer-to-peer lending facilitators, crowd-funding providers and specialist mortgage lenders. These participants are active within the consumer and corporate lending markets and focus on niche areas where larger banks have typically chosen not to operate. In addition, foreign banks, investment banks, insurance and life assurance companies have at various times been active in UK personal financial services, particularly the mortgage and retail savings markets, and a number of companies have expressed a desire to enter the market. Price-based competition has increased as institutions increasingly use low-cost telephone, mail and internet-based distribution channels (including via mobile banking) to offer competitively priced retail savings accounts, mortgages and other financial products. The internet as a distribution channel provides significant opportunities for further competition from both new and existing banking entrants. The market for financial services has also been impacted by the increasing use of internet aggregator websites that provide speedy comparison of financial products and prices. The use of the intermediary sector also allows new entrants to gain access to the UK mortgage market.

### 3. THE UK RESIDENTIAL MORTGAGE MARKET

The following table sets out the total balances of UK lending secured on residential property and the proportions held by building societies, banks and the Society, as at 30 September 2017 and as at 31 December 2016, 2015 and 2014.

	<b>Total balances</b>	<b>Building societies</b>	<b>Banks</b>	<b>Others</b>	<b>Society's share of total UK residential mortgages</b>
	<i>(£ billions)</i>				
2017 <sup>(to 30 September)</sup> .....	1,385.6	21.9%	66.4%	11.7%	0.32%
2016.....	1,322.6	21.5%	65.9%	12.5%	0.32%
2015.....	1,288.4	20.7%	65.6%	13.7%	0.32%
2014.....	1,255.9	20.0%	65.7%	14.3%	0.31%

Source: Bank of England research, except for information regarding the building society balances which are taken from Building Society Association data, and information regarding the Society's balances which are taken from the Society's own data supplied to the Bank of England.

The overall size of the new residential mortgage market in the UK has shrunk considerably since the year to 31 December 2007 when gross new mortgage lending totalled approximately £351 billion. For the year to 31 December 2016, the equivalent figure was approximately £245 billion, in each case according to BoE data. The first 9 months of 2017 had seen an increase in mortgage lending activity compared to the corresponding period in the previous year, with lending of £194 billion. However, the nature of competition is essentially unchanged with competition for new lending business remaining fierce. The majority of this is for residential purposes; there has been a softening in the buy to let market following stamp duty and other taxation reforms and in response to changes in underwriting standards. In recent years, based on English Housing Survey data, there has been a decline in the proportion of people owning their own homes, from a peak of around 71 per cent. in 2003 to 62 per cent. in 2017. The impact of the global financial crisis is still evident in the mortgage market, with fewer products available which permit high loan to value (LTV) ratios, although this has begun to change in recent years.

The following tables set out gross and net UK lending secured on residential property and the proportions advanced by building societies, banks and the Society, for the year 9 months to 30 September 2017 and each of the years ended 31 December 2016, 2015 and 2014. For these purposes, gross lending is all advances (including for house purchase, remortgage and buy to let) and net lending is gross lending less principal repaid.

	<b>Gross UK residential mortgages advanced</b>	<b>Building societies (including the Society)</b>	<b>Banks</b>	<b>Others</b>	<b>Society's share of gross UK residential mortgages advanced</b>
	<i>(£ billions)</i>		<i>(per cent.)</i>		
2017 <sup>(to 30 September)</sup> .....	194.0	25.7%	67.0%	7.3%	0.32%
2016.....	245.1	27.1%	65.1%	7.8%	0.30%
2015.....	221.8	25.7%	64.2%	10.1%	0.26%
2014.....	203.4	25.9%	65.0%	9.1%	0.22%

Source: Bank of England research and Building Societies Association, except for information regarding the Society's lending, which is taken from the Society's own data supplied to the Bank of England and the Building Societies Association.

A feature of the mortgage market in the UK is the differential pricing structure that has developed in response to increased competition. New customers are offered attractive interest rates in the form of discounts or cash-backs for an initial period of time (referred to as "frontbook" rates), at lower rates rather than lenders' standard (or "backbook") interest rates. For October 2017 remortgage activity totalled an estimated £7.3 billion. In the year to 31 December 2016, remortgaging totalled an estimated £66.3 billion, up 21 per cent. on the year to 31 December 2015 (source: UK Finance).

#### 4. THE UK RETAIL SAVINGS MARKET

The following table sets out the total balance of UK retail savings held by building societies, banks, National Savings and Investments, the Government-owned funding agency (NS&I) and the Society, as at 30 September 2017 and as at 31 December 2016, 2015 and 2014.

	<b>Total balances</b>	<b>Annual rate of growth</b>	<b>Building societies (including the Society)</b>	<b>Banks and other<sup>(1)</sup></b>	<b>NS&amp;I</b>	<b>Society's share of total UK retail savings</b>
	<i>(£ billions)</i>			<i>(per cent.)</i>		
2017 <sup>(to 30 September)</sup> .....	1,458.3	3.3%	18.3%	71.4%	10.3%	0.29%
2016.....	1,427.9	6.1%	18.4%	71.6%	10.0%	0.30%
2015.....	1,346.1	5.2%	18.3%	71.7%	10.0%	0.32%
2014.....	1,279.4	4.4%	18.7%	72.6%	8.7%	0.32%

Note:

(1) Comprises the total less building societies and NS&I.

Source: Bank of England and Building Societies Association, except for information regarding the Society's retail savings, which is taken from the Society's own data supplied to the Bank of England. Building society figures also include the Society's own data.

The total balance of UK retail savings was £1,458 billion as at 30 September 2017. At 31 December 2016 the total balance was £1,428 billion with balances having grown by 6.1 per cent. over the level as at 31 December 2015 and by an annual 5.2 per cent. over the level as at 31 December 2014, according to BoE data.

In the last few years, competition for UK retail deposits has increased as new participants, such as foreign banks, supermarkets, insurance and life assurance companies, challenger banks and direct online banking providers have entered the market by offering attractive rates of interest. These new entrants have caused the cost of attracting new retail deposits to increase for existing participants in the market and have impacted the flow of new retail deposits. The Society believes that increased consumer awareness driven by the press and increased competition has created potentially greater volatility of retail deposit balances both between different organisations and between different accounts within organisations. This, in turn, has resulted in a reduction in the differential between rates paid on existing and new balances as customers transfer to high rate accounts and organisations aim to retain existing balances.



## PART XII - DESCRIPTION OF THE SOCIETY'S BUSINESS

### 1. OVERVIEW

West Bromwich Building Society (the **Society**) was formed as a mutual organisation – owned and run for the benefit of its members - in 1849, with the aim of helping people to better themselves through savings and the security of owning their own homes.

The Society is the leading regional building society in Birmingham and the Black Country, and the 7th largest in the UK by assets under management (approximately £5.7 billion as at 30 September 2017) with circa 446,000 members. The Society is a major provider of financial products and services, notably prime residential mortgages, savings and investments, employing approximately 760 staff and has an extensive network of 37 branches across the Black Country and Birmingham, as well as a presence around the mid-Wales border and Shropshire.

As a traditional, regional building society the Society remains committed to the principles of mutuality and all decision-making is centred around the delivery of long-term value to its circa 446,000 members. The Society 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 2016/17 financial year, the Society invested substantially in the mortgage application and customer management systems to make it easier for members to do business with the Society and to provide operational efficiencies.

Following its re-entry into the mortgage market in 2012 the Society has received external recognition and service awards including:

**Financial Adviser Service Awards** - Development of the intermediary strategy to support future growth – received a five star rating, the highest accolade possible, for the 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.

**Mortgage Finance Gazette Awards** - Strong support for the Society's 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.

### 2. STRATEGY

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

In delivering the savings and investments offering, the Society aims to provide security, simplicity and value to its members. The Society strives to meet the needs of its members with a competitive range of products that offers transparency and clarity, delivering good returns. The Society continues to invest in the main systems to make it easy for members to access products and services.

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

Whilst the Society has made significant progress with its strategy over the last few years, the Society still plans to manage down its 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.

### ***Strategic priorities***

The Society's strategic priorities are:

- **Security**
  - Generate and maintain sufficient capital and liquidity to enable the Society to deliver its business plans.
  - Continue to exit the Society's legacy positions whilst balancing speed with the economic cost.
  - Have a clear, transparent approach to risk management.
- **Members**
  - Make decisions that are in the interests of the Society's current and future membership as a whole.
  - Consider the impact of actions on customer outcomes, customer experience and other stakeholders.
- **Efficiency**
  - Delivery of member value underpins all components of the Society's operating model.
  - Existing resources are leveraged to deliver acceptable returns.
  - Seek to exploit technology at every stage of the operating model to reduce the cost of service delivery.

## **3. HISTORY OF THE SOCIETY**

Building societies have existed in the UK for over 200 years. From the outset, they were community-based, cooperative organisations created to help people purchase homes. The main characteristic of building societies is their mutual status, meaning that they are owned by their members, who are primarily retail savings and residential mortgage customers. The Society's origins date back to April 23, St George's Day, 1849 with the setting up of the West Bromwich Permanent Building Society. The Society's early objectives were clear – 'to enable its members to acquire property by the fruits of their own honest industry and frugality from a common fund raised by members' contributions', together with the facility to provide the 'safe deposit of money in large or small sums as either temporary or permanent investments.' Although there has been significant growth and expansion of activities and modernisation over the decades, these original objectives remain at the core of the Society's values.

The Society's brand identity was refreshed in 2010, along with a change of trading name to the West Brom. The new brand was introduced to all branches as part of a major modernisation programme. Several branches were moved to better locations in their respective towns to create more space for counter points and additional private consultation rooms. In the wake of the credit crunch, which had a significant impact on the whole of the financial services sector, the Society adopted a back-to-basics approach and stepped away from more diverse activities such as commercial lending. Its focus was squarely on the traditional building society practices of providing a safe home for savers' money and making funds available to those who wish to purchase their own homes.

2016 marked another milestone for the Society as it moved into its new purpose-built headquarters at Providence Place. Located in West Bromwich, the building is seen as a visual statement of the Society's connection with its past and its promise of a forward-thinking future.

#### 4. RECENT DEVELOPMENTS

##### Buy to let decision & continued progress

In 2013 the Board took the decision to increase the interest rate paid by multi-property landlords, the vast majority of whom were not members of the Society. This decision was taken to address the position of members given the low returns being suffered by the Society's saving members in the unprecedented low interest rate environment. The action was taken on the basis of clear and unambiguous legal advice but its legality was challenged in the UK courts. In June 2016 the Court of Appeal issued a judgment on the matter, overturning a previous High Court ruling in favour of the Society. The Society duly met its obligations and ceased to charge the additional interest and reimbursed affected borrowers for what had previously been levied. The financial impact included a one-off cost of £27.5 million incurred by the Society, reflected in the loss before tax reported for both the full and half year 2016/17.

In the first half of the current financial year (2017/18), the Society reported an unaudited statutory and underlying profit before tax of £4.2 million (30 September 2016: statutory loss of £23.7 million, underlying profit of £3.8 million), with continued growth in prime residential lending advances and non-core commercial assets reduced further.

##### Modernisation of the Society's Capital Structure

In February 2017, the Society announced that it was seeking clarification from the EBA in relation to the eligibility of its PPDS as CET1 capital, following an investor challenge.

While the Society continues to believe that the PPDS met the CET1 criteria in all respects, the Society in the meantime had constructive engagement with major holders of both the PPDS and the PIBS with respect to its options. It was clear throughout discussions with these major holders that, irrespective of the outcome of the EBA's deliberations on eligibility of the PPDS, the major holders and the Society were aligned in their views that a modernisation of the Society's capital structure would be appropriate.

Following these discussions, the Society announced on 13 December 2017 its plans to conduct a liability management exercise (the **LME**) involving its PPDS and the PIBS. The Society launched the LME on 8 March 2018, and announced the final results of the LME on 10 April 2018. The Society expects the LME to settle on 12 April 2018.

#### 5. GROUP STRUCTURE AND PRINCIPAL SUBSIDIARIES

The Society has three main subsidiaries; West Bromwich Mortgage Company Limited, West Bromwich Homes Limited and West Bromwich Commercial Limited. The Society holds the interests directly (unless otherwise stated) for key subsidiary undertakings, all of which are registered in England.

The Society's interests in its principal subsidiary undertakings, all of which are consolidated, as at 31 March 2017 are set out below:

Wholly-owned subsidiary undertakings	Nature of business
West Bromwich Mortgage Company Limited	Residential mortgage lending
West Bromwich Commercial Limited	Commercial mortgage lending
CL Mortgages Limited	Residential mortgage lending

West Bromwich Homes Limited	Investment in property for rental
Insignia Finance Limited	Second charge lending
White Label Lending Limited	Second charge lending

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

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

The Society is the principal holding entity of the Group and the main business of the Group is conducted by the Society.

The Society also has interests in structured entities. A structured entity is an entity in which voting or similar rights are not the dominant factor in deciding control. Structured entities are consolidated when the substance of the relationship indicates control.

The table below provides details of these entities as at 31 March 2017.

<b>Group undertaking</b>	<b>Principal Activity</b>	<b>Country of Incorporation</b>
Sandwell Commercial Finance No. 1 Plc	Securitisation entity	UK
Sandwell Commercial Finance No. 2 Plc	Securitisation entity	UK
Hawthorn Asset Co Limited	Securitisation entity	UK
Hawthorn Finance Limited	Securitisation entity	Jersey
Kenrick No. 1 Plc	Securitisation entity	UK
Kenrick No. 2 Plc	Securitisation entity	UK

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.

## **6. BUSINESS MODEL**

### **Introduction**

The Society's strategic aims have resulted in a business model split between core and non-core activities. Emphasis is placed on the core activities of retail savings, investments and prime residential lending meaning that the Society is 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 the Society's 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, although lending to commercial entities for residential property investments will continue; 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.

### Overview by business division

The following table sets out the underlying profit/(loss) relating to the Society's business divisions for the financial year ended as at 31 March 2017.

	2017	2016	2015
	£m	£m	£m
Retail	10.6	2.9	1.5
Commercial	(9.3)	(4.3)	(5.6)
Property	6.4	6.5	5.9
Intercompany Adjustments	-	(0.3)	(1.1)
<b>Total underlying profit before tax</b>	<b>7.7</b>	<b>4.8</b>	<b>0.7</b>

Source: The Society's Annual Report and Accounts FY 2017, FY 2016 (underlying profit refers to profit before tax restated to remove additional interest charged following the buy to let court decision referred to at section 4 (*Recent Developments*) above)

### Retail business division

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

After removing the impact of the buy to let interest refund following the court decision referred to at section 4 (*Recent Developments*) above, Retail performance markedly improved in the year ended 31 March 2017 with an underlying profit before tax of £10.6 million (FY 2016: £2.9 million). A 15% growth in prime residential mortgage balances, as a result of completions of £712 million (FY 2016: £673 million), made a positive contribution to the segment result, as did a £3.5 million reduction (FY 2016: £0.2 million 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 during the year ended 31 March 2017, with just 0.81% of residential mortgage accounts three months or more past due at 31 March 2017 (31 March 2016: 1.27%).

### *Residential mortgage 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 (31 March 2016: 49.8%), 42.6% buy to let (31 March 2016: 48.0%) and 1.9% other (31 March 2016: 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.

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.

The table below shows the geographical distribution of the Society's UK residential mortgage loans as at 31 March 2017.

	<b>UK residential mortgage lending to individuals as at 31 March 2017</b>
	<i>(per cent.)</i>
<b><u>Region</u></b>	
East Anglia .....	2.9
East Midlands .....	9.8
Greater London.....	13.1
Northern Ireland .....	0.1
North.....	3.9
North West.....	11.7
Scotland .....	2.7
South East.....	17.7
South West.....	8.3
Wales .....	4.9
West Midlands.....	16.7
Yorkshire .....	8.2
<b>Total.....</b>	<b>100.0</b>

Source: The Society's Annual Report and Accounts 2017.

The Society offers a range of competitive and 'Best Buy' mortgage deals, including incentives such as free valuations and cashbacks, via its branch, direct and intermediary channels.

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.

The table below shows the Society's residential mortgage loans which were three months or more in arrears as a percentage of its total residential mortgage loans as at each of 31 March 2017, 31 March 2016 and 31 March 2015.

	As at 31 March		
	2017	2016	2015
	<i>(per cent.)</i>		
Prime Owner Occupied .....	0.70	0.96	1.44
Buy to let .....	0.30	0.90	0.98
Other .....	6.81	8.19	8.88
<b>Core Residential</b> .....	<b>0.63</b>	<b>1.07</b>	<b>1.34</b>
Second Charge Lending.....	8.58	8.58	10.34
<b>Total residential</b> .....	<b>0.81</b>	<b>1.27</b>	<b>1.63</b>

Source: The Society's Annual Report and Accounts 2017 and 2016.

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% (31 March 2016: 1.27%) of accounts were three months or more in arrears. This compares favourably with data from the Council of Mortgage Lenders (CML) which showed that the average number of accounts greater than three months in arrears, as a percentage of total accounts, was around 1.0% for the 2016 calendar year. Excluding the closed second charge lending portfolio, the residential arrears percentage was lower still at 0.63% (31 March 2016: 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 comprehensive pricing models and strict affordability criteria ensure that all new lending is undertaken within the Board's credit risk appetite.

### ***Savings***

Aligned to the principles of mutuality, the Society is primarily funded by retail deposits, with residential mortgage assets amply covered 1.04 times by retail savings balances as at 31 March 2017 (31 March 2016: 1.06 times). The retail savings book marginally increased during the year to £4.43 billion (31 March 2016: £4.39 billion), with 60% (31 March 2016: 59%) held in branch-based accounts.

During the 2016/17 financial year, the Society 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.

### ***Other income***

The Society's 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.

As at 31 March 2017 Other income was £6.8 million (31 March 2016: £7.6 million; 31 March 2015: £8.0 million), including £4.1 million (31 March 2016: £4.1 million; 31 March 2015: £4.0 million) 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.

### Commercial business division

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. However, lending to commercial entities for residential property investments will continue.

During the 2016/2017 financial year, commercial mortgage balances fell 14% to £588 million (31 March 2016: £680 million; 31 March 2015: £835 million) of which £73 million was securitised (31 March 2016: £92 million; 31 March 2015: £130 million) with full provision made for the residual risk to the Group.

The table below analyses the commercial loan balances by industry type as at 31 March 2017, 31 March 2016 and 31 March 2015:

	as at 31 March		
	2017	2016	2015
	(£m)	(£m)	(£m)
Healthcare and leisure .....	139.4	167.0	186.4
Industrial and warehouse .....	23.3	23.1	34.9
Office.....	35.1	48.7	117.6
Retail .....	305.4	350.2	395.7
Residential property.....	18.7	20.2	22.9
Other .....	21.3	21.4	23.0
Fair value adjustments .....	44.3	49.0	54.6
<b>Total.....</b>	<b>587.5</b>	<b>679.6</b>	<b>835.1</b>

Source: The Society's Annual Report and Accounts 2017 and 2016

Certain commercial property sectors remain volatile and, during FY 2017, impairment charges rose to £11.1 million, compared with £7.9 million in FY 2016. This led to a decline in segment performance and an underlying loss before tax of £9.3 million (FY 2016: £4.3 million).

The overall exposure to assets secured on commercial properties has fallen from £1.7 billion at 31 March 2008 to £0.6 billion at 31 March 2017.

### Property business division

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 £5.4 million was reported for the West Bromwich Homes Limited residential property portfolio at 31 March 2017 (31 March 2016: £5.5 million; 31 March 2015: £5.5 million), as a result of house price inflation during the year. The carrying value of the portfolio at 31 March 2017 was £128.9 million (31 March 2016: £123.7 million; 31 March 2015: £118.6 million). One property was sold during the 2016/17 year achieving its book value of £0.2 million, with 4 properties sold the previous financial year achieving their book value of £0.4 million. Eleven properties were sold during FY 2016, also achieving their book value of £2.1 million.



## **7. MANAGEMENT EXPENSES AND INVESTMENTS**

Management expenses increased in FY 2017 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 £5.1 million to £5.7 million for 2016/17.

During FY 2017, the Society made further investment in core systems to enable growth and with a view to assuring the ongoing provision of excellent customer service. Efficiency savings of circa £1 million 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 during FY 2017 from £42.0 million to £44.4 million 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 FY 2017 was 0.86% (FY 2016: 0.83% and FY 2015: 0.76%).

The Society continues to invest in systems designed to improve the customer experience, as well as moving forwards with the IRB approach to credit risk capital requirements – a regulatory project which the Society expects, due to the low risk nature of the Society's core mortgage books, may improve the Society's already robust capital position.

## **8. FSCS**

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

As at 31 March 2017 the Society held a provision of £0.8 million representing 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.

## PART XIII - DIRECTORS, EMPLOYEES AND CORPORATE GOVERNANCE

The affairs of the Society are conducted and managed by a Board of Directors (the **Board**) who are responsible for the Society's strategy and are elected and serve in accordance with the Society's Rules and Memorandum. The Board is responsible to the members for the proper conduct of the affairs of the Society and in turn appoints and monitors executives who are responsible for the daily management of the Society.

The business address of the Society's Directors is at 2 Providence Place, West Bromwich B70 8AF. There are no potential conflicts between the duties to the Society of the Directors and their private interests and/or other duties.

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.

### 1. DIRECTORS

The following table presents information with respect to current Directors:

Name	Age	Position	Other directorships and interests
Mark Nicholls	68	Chairman and Non-Executive Director	Northern Investors Company PLC Rathbone Brothers Plc Rathbone Investment Management Ltd
Jonathan Westhoff	53	Chief Executive	West Bromwich Commercial Limited West Bromwich Homes Limited West Bromwich Mortgage Company Ltd CL Mortgages Limited
Mahomed Ashraf Piranie	54	Group Finance & Operations Director	Elite Star Investment Limited Osborne House Property Management Ltd DPC (2011) Limited West Bromwich Mortgage Company Ltd CL Mortgages Limited
Julie Hopes	50	Non-Executive Director	Co-op General Insurance Police Mutual Assurance Society
Mark Preston	58	Non-Executive Director	Acenden Limited Kensington Mortgage Company Ltd
Martin Ritchley	71	Deputy Chairman, Senior Independent Director and Non-Executive Director	Royal Shakespeare Theatre Trust
Richard Sommers	61	Non-Executive Director	Sidmouth Rugby Football Club Limited Al Rayan Bank PLC
Stuart James Turner	48	Non-Executive Director	Prudential Plc
Colin Walklin	63	Non-Executive Director	Standard Life Investments (Holdings) Limited Standard Life Investments Limited Standard Life Portfolio Investments Limited Standard Life Wealth Limited Standard Life Overseas Holdings Limited Standard Life Employee Services Limited

**Mark Nicholls MA (Cantab), MBA**

*Chairman and Non-Executive Director*

*Date of appointment to the Board: 1 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.

***Jonathan Westhoff BA (Hons) Financial Services, FCMA, CGMA, ACIB***

*Chief Executive*

*Date of appointment to the Board: 5 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.

***Mahomed Ashraf Piranie FCCA, MBA***

*Group Finance & Operations Director*

*Date of appointment to the Board: 13 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 Society, 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.

***Julie Hopes MBA, ACIB***

*Non-Executive Director*

*Date of appointment to the Board: 1 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 Preston BA (Hons), ACIB***

*Non-Executive Director*

*Date of appointment to the Board: 18 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 Chair of the Risk Committee and a member of the Audit and Remuneration committees.

***Martin Ritchley FCA, FCIB, Hon DBA (Coventry)***

*Deputy Chairman, Senior Independent Director and Non-Executive Director*

*Date of appointment to the Board: 1 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***

*Non-Executive Director*

*Date of appointment to the Board: 1 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 of the University of Oxford, before retiring in 2016, and is now an Emeritus Fellow. Richard is a member of the Risk, Audit and Nominations committees.

***Stuart James Turner FCA, FCSI, BA (Hons)***

*Non-Executive Director*

*Date of appointment to the Board: 1 April 2017*

James is the Group Chief Risk Officer and Executive Director at Prudential plc, having previously been Director of Group Finance. 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***

*Non-Executive Director*

*Date of appointment to the Board: 20 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.

## **Directors' compensation**

For the financial year ended 31 March 2017 the aggregate amount of compensation that the Society paid to all directors and executive officers as a group totalled £1.62 million.

The Remuneration Policy (the **Policy**) provides the framework for the Remuneration 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. In addition to a basic salary the Executive Directors receive performance related pay linked to the delivery of Society and personal objectives, with a maximum annual opportunity of 50% of basic salary. In addition 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.

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.

### Management employee pension schemes

Executive Directors are invited to join the Society's stakeholder pension plan or, as an alternative, be provided with a cash allowance of up to 25% of salary.

## 2. EMPLOYEES

The following table sets out the average number of persons employed by the Society at both a group and Society level during each of the financial years ended 31 March 2017, 31 March 2016 and 31 March 2015.

	Group			Society		
	2017	2016	2015	2017	2016	2015
Full time.....	620	616	614	613	609	605
Part time.....	138	124	111	137	123	111
<b>Total .....</b>	<b>758</b>	<b>740</b>	<b>725</b>	<b>750</b>	<b>732</b>	<b>716</b>
Central administration .....	535	490	472	535	490	472
Branches .....	215	242	244	215	242	244
Subsidiaries.....	8	8	9	—	—	—
<b>Total .....</b>	<b>758</b>	<b>740</b>	<b>725</b>	<b>750</b>	<b>732</b>	<b>716</b>

## 3. 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.

The Society is run on a day to day basis by its Senior Management Team, and governed by a Board which consists of both Executive and 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.

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. The Chief Executive has overall responsibility for managing the Society and implementing Board agreed strategy. This clear division of responsibility helps to ensure that no one individual has unfettered powers of decision-making and influence.

## 4. MATTERS RESERVED FOR THE BOARD

The Society's Board acts in what the directors consider as being in the best interests of the Society's members, consistent with the statutory and regulatory duties.

### Strategy and Management

**The Board is responsible for:**

- The entrepreneurial leadership of the Society.
- Setting the Society's:
  - Values;
  - Risk appetite;
  - Strategic aims; and
  - Annual objectives.
- Approval of the annual operating and capital expenditure budgets and any material changes to them.
- Oversight of the Group's operations ensuring:
  - Competent and prudent management;
  - Sound planning and risk management;
  - An effective system of internal control;
  - Adequate accounting and other records;
  - Compliance with statutory and regulatory obligations; and
  - Adequate financial and human resources.
- Review of performance in the light of the Group's strategy objectives, business plan and budgets and ensuring that any necessary corrective action is taken.
- Extension of the Group's activities into new business or geographic areas.
- Any decision to cease to operate all or any material part of the Group's business.
- Approve the Society's Recovery and Resolution Plan.

**Structure and Capital**

- The Board is responsible for approving:
  - Changes to the Group's capital structure;
  - Major changes to the Group's corporate structure;
  - Changes to the Group's management and control structure; and
  - Any changes to the Society's mutual status.

**Financial Reporting and Controls**

- Approval of preliminary announcement of the interim and final results.

- Approval of the annual report and accounts including the Corporate Governance statement and remuneration report.
- Approval of any significant changes in accounting policies or practices.
- Approval of Pillar 3 Disclosures.
- Approval of Treasury and Financial Risk Management Policy.
- Approval of ICAAP and ILAAP.
- Approval of Regulatory costs.
- Approval of PIBS payments.

#### **Internal Controls**

- Ensuring maintenance of a sound system of internal control and risk management including:
  - Receiving reports on, and reviewing the effectiveness of, the Group's risk and control processes to support its strategy and objectives;
  - Undertaking an annual assessment of these processes;
  - Approving an appropriate statement for inclusion in the annual report; and
  - Approval of the Society Risk Appetite Statements.

#### **Contracts**

- To consider and approve the business case/contract where the value or cost of the initiative will exceed £500k over the life of the initiative.

#### **Communication**

- Approval of resolutions and corresponding documentation to be put forward to members at annual general meetings.
- Approval of all circulars, prospectuses and listing particulars.

#### **Board Membership and Other Appointments**

- Changes to the structure, size and composition of the Board.
- Ensuring adequate succession planning for the Board and Senior Management.
- Appointments to the board, following recommendations by the Nomination Committee.
- Selection of the Chairman of the Board and the Chief Executive.
- Appointment of the Senior Independent Director.
- Membership and Chairmanship of Board Committees.
- Continuation in office of directors at the end of their term of office when they are due to be re-elected at the AGM and otherwise as appropriate.

- Appointment or removal of the company secretary.
- Appointment, reappointment or removal of the external auditor to be put to members for approval, following the recommendation of the Audit Committee.
- Appointment of SRS (Staff Retirement Scheme) Chairman.

#### **Delegation of authority**

- Approval of terms of reference of Board committees.
- Approval of the Board Authorised Signatories list.
- Receiving reports from Board committees on their activities.

#### **Corporate Governance Matters**

- Undertaking a formal and rigorous review annually of its own performance, that of its committees and individual directors.

#### **Policies**

Approval of policies, including:

- Business Continuity Policy;
- Risk Management Framework;
- Health and Safety Policy;
- Product Governance Framework;
- Remuneration Policy;
- Residential Lending Statement;
- Responsible Lending Policy; and
- Treasury and Financial Risk Management Policy.

#### **Lending**

- To approve residential loans made by the Society, including the acquisition of mortgage portfolios, where the aggregated counterparty commitment exceeds £2 million.
- To approve commercial and/or investment property loans where the aggregated counterparty commitment exceeds £2.5 million.
- To approve new syndicated loan arrangements.
- To approve new buy-to-let loans made by the Society when the loan exceeds £1.5 million and further advances to existing buy-to-let portfolios when the individual further advance for a specific property exceeds £0.5 million or the total advanced to any one customer exceeds £1.5 million.

#### **Financial**



- To consider and approve an Annual Budget for management expenses and capital and revenue expenditure, for the Society and each of its subsidiary companies.
- To approve budgeted revenue or capital expenditure exceeding £1 million (£250k if unbudgeted) whether in respect of individual or linked transactions.
- To approve the acquisition/disposal of any provisions exceeding £500k (or lease equivalent) whether in respect of individual or linked transaction.
- Through the Remuneration Committee to approve overall salary costs, any performance related pay awards, Annual Salary Review and Pension Scheme funding.
- To authorise the reimbursement of accounts following losses incurred as a result of fraud, where the sum involved exceeds £100k; to authorise the provision of fraud indemnities to other building societies and banks, where the sum involved exceeds £100k.
- Approve of any changes in accounting policies and practices.
- Approve the opening and closure or relocation of branch offices/head office/administration centres.
- To approve any aggregated mortgage loss exceeding £5 million.
- To take note of the annual Client Asset Disclosure.

#### **Rules and Member Nominations/Resolutions**

- To agree proposals to be put to Members for amendments to the Memorandum and Rules of the Society.
- To consider nominations for Director and Resolutions submitted by Members and, subject to the Memorandum and Rules and any legal advice, approve putting such nominations/resolutions to a General Meeting of members.
- To approve AGM and SGM communications issued to members.

#### **Products**

- To approve new initiatives/channels.

#### **Mergers/Acquisitions**

- To approve any merger/conversion activity.
- To approve the acquisition of any business activity requiring the establishment of a subsidiary or the disposal of any subsidiary.

#### **Other**

- Review and approval of this schedule of authorities reserved to the Board.
- Approve of the overall levels of insurance for the Society, including Directors' and Officers' liability insurance and indemnification of Directors.

- Approve the general approach on the use of litigation and major decisions on any particular piece of litigation capable of having a substantial financial bearing or impact on the reputation of the Society or its subsidiary companies.
- Approve the introduction or withdrawal of non-core member services, but not minor changes to existing product lines.
- Review and approval of the annual Health and Safety Report.
- To recognise/derecognise staff representative bodies.

## **5. BOARD COMMITTEES**

In addition to those matters reserved to the Board, a number of committees exist to complement the Board's activities and to ensure the Society follows best practice in corporate governance matters. Certain responsibilities of the Board have been delegated to these Committees.

Further details of the Audit Committee, the Remuneration Committee, the Risk Committee and the Nomination Committee are set out below:

### ***The Audit Committee***

This Board committee (amongst other matters):

- Provides the Board with assurance regarding the integrity of the financial statements and associated documents;
- Ensures the adequacy and effectiveness of the Society's internal control systems;
- Ensures the effectiveness of the Society's Internal Audit function; and
- Ensures the effectiveness of the Society's external auditors.

### ***The Remuneration Committee***

This Board committee (amongst other matters):

- Develops and recommends remuneration policy; and
- Makes recommendations in respect of remuneration arrangements for Executive Directors and other Code Staff.

### ***The Risk Committee***

This Board committee (amongst other matters):

- Oversees the development, implementation and maintenance of the Society's risk management framework, including its risk appetite statements and metrics to ensure they are appropriate and align with business strategy, current and emerging regulatory, corporate governance and industry best practice;
- Reviews the processes and procedures for ensuring that all material and business risks are properly identified and appropriate systems of assessing, monitoring and controls are in place;
- Receives and reviews management reports which assess the nature and extent of the current and emerging risks facing the Society;

- Reviews annually the Society's Risk Management Framework Document, Policy Governance Framework and Credit Risk Policies; and
- Oversees the effectiveness and independence of the Society's Risk and Compliance functions.

#### *The Nomination Committee*

This Board committee (amongst other matters):

- Recommends appointments and re-appointments of Directors to the Board;
- Recommends the composition of Board Committees to the Board;
- Reviews the structure, size and composition of the Board; and
- Reviews Society statements relating to Corporate Governance.

The Society has allocated positions with Senior Management Responsibilities in accordance with the Senior Managers Regime which came into force on 7 March 2016.

All committees review their own performance and terms of reference annually to ensure they are operating at maximum effectiveness, and recommend any changes considered necessary to the Board.

## PART XIV - CAPITALISATION AND INDEBTEDNESS

The following tables set out a summary of the Society's unaudited consolidated capitalisation as at 31 March 2017 and its unaudited financial indebtedness as at 30 September 2017, each prepared under IFRS using policies which are consistent with those used in the Consolidated Historical Financial Statements.

### Consolidated capitalisation

The financial information in the table below relating to the Society's consolidated capitalisation as at 31 March 2017 has been extracted without material adjustment from the Consolidated Historical Financial Statements. Although, as a mutual organisation owned by its members, the Society does not have equity shareholders, share capital or capital reserves, it has issued other instruments which are accounted for as equity securities and information relating to these is included in the table below.

	As at 31 March 2017
<b>Equity securities</b>	<b>£m</b>
Profit participating deferred shares <sup>(1)</sup> .....	173.0
Additional tier 1 instruments <sup>(2)</sup> .....	75.0
<b>Total capitalisation</b> .....	<b>248.0</b>

Notes:

- (1) A form of unsecured capital that are included as Common Equity Tier 1 capital. PPDS rank behind the claims of all depositors, payables, investing members of the Society and PIBS holders.
- (2) Subscribed capital in the form of interest bearing shares. In a winding up or dissolution of the Society the claims of the holders of PIBS would rank behind all other creditors of the Society, with the exception of the claims of holders of PPDS. The holders of PIBS are not entitled to any share in any final surplus upon winding up or dissolution of the Society.

As at the date of these Listing Particulars, there has been no material change to the quantum of the Society's profit participating deferred shares or additional tier 1 instruments since 31 March 2017. However, as a result of the LME, the Society expects that, following the scheduled settlement date of 12 April 2018:

- the PPDS will cease to be outstanding;
- the nominal amount outstanding of the PIBS will be reduced to £8,891,000;
- the Society will have issued 1,288,813 CCDS, corresponding to £128,881,300 at the issue price of £100 per CCDS; and
- the Society will have issued £22,498,600 principal amount of Tier 2 Notes.

The Society is not aware of any natural or legal persons who/which, directly or indirectly, severally or jointly, exercise or could exercise control over the Society, and, due to the nature of the Society as a mutual organisation, where each member receives one vote regardless of the size of the member's deposit account, mortgage loan or shareholding or the number of accounts the member maintains, there are no members of the Society who, directly or indirectly, hold 10% or more of the Society's capital or voting rights.

For information on the Society's capital position, see "*Part XVII: Capital Adequacy*".

### Consolidated financial indebtedness

The table below sets out the Society's consolidated financial indebtedness as at 30 September 2017. As the taking of deposits is part of the core business of the Society, this table does not classify deposits as indebtedness.

	<b>As at 30 September 2017</b>
	<i>(£m)</i>
<b>Consolidated indebtedness</b>	
Debt securities in issue <sup>(1)</sup> .....	169
<b>Total senior debt</b> .....	<b>169</b>

Notes:

- (1) The non-recourse finance comprises mortgage backed floating rate notes (the **MB Notes**) secured over portfolios of mortgage loans secured by first charges over residential and commercial properties in the UK. Prior to redemption of the MB Notes on the final interest payment date, the MB Notes will be subject to mandatory and/or optional redemption, in certain circumstances, on each interest payment date.

## PART XV - SELECTED FINANCIAL INFORMATION

The following tables set out selected consolidated information which has been derived from the Consolidated Historical Financial Statements. All data in this section should be read in conjunction with the Consolidated Historical Financial Statements and the H1 2017/8 Interim Financial Statements as well as “*Part XVI: Operating and Financial Review*”:

### INCOME STATEMENT DATA

	Financial year ended 31 March		
	2017	2016	2015
		(£m)	
Interest receivable and similar income .....	108.9	126.7	136.9
Interest expense and similar charges .....	(53.6)	(66.7)	(72.2)
<b>Net interest receivable .....</b>	<b>55.3</b>	<b>60.0</b>	<b>64.7</b>
Fees and commissions receivable .....	2.7	3.7	4.2
Other operating income .....	4.1	3.9	3.8
<b>Total operating income .....</b>	<b>62.1</b>	<b>67.6</b>	<b>72.7</b>
Fair value losses on financial instruments .....	(0.2)	(1.0)	(16.3)
Net realised profits.....	0.5	0.6	0.1
<b>Total income.....</b>	<b>62.4</b>	<b>67.2</b>	<b>56.5</b>
Administrative expenses.....	(44.4)	(42.0)	(40.6)
Depreciation and amortisation.....	(5.7)	(5.1)	(5.4)
<b>Operating profit before revaluation gains, impairment and provisions .....</b>	<b>12.3</b>	<b>20.1</b>	<b>10.5</b>
Gains on investment properties .....	5.4	5.5	5.5
Impairment on loans and advances .....	(7.6)	(8.1)	(0.2)
Provisions for liabilities .....	(29.9)	(4.0)	(3.4)
<b>(Loss)/Profit before tax .....</b>	<b>(19.8)</b>	<b>13.5</b>	<b>12.4</b>
Taxation.....	(6.0)	(4.1)	(3.2)
<b>(Loss)/Profit for the financial year .....</b>	<b>(25.8)</b>	<b>9.4</b>	<b>9.2</b>

# STATEMENT OF COMPREHENSIVE INCOME

	Financial year ended 31 March		
	2017	2016	2015
		(£m)	
<b>(Loss)/Profit for the financial year</b>	<b>(25.8)</b>	<b>9.4</b>	<b>9.2</b>
<b>Other comprehensive income</b>			
<b>Items that may subsequently be reclassified to profit or loss</b>			
Available for sale investments			
Valuation gains/(losses) taken to equity....	0.5	(2.2)	(1.0)
Amounts transferred to Income Statement.	(0.5)	(0.6)	(0.1)
Cash flow hedge losses taken to equity	(0.5)	(0.2)	(0.3)
Taxation.....	0.1	0.2	0.2
<b>Items that will not subsequently be reclassified to profit or loss</b>			
Gains on revaluation of land and buildings....	0.6	-	-
Actuarial losses on defined benefit obligations	(10.4)	(0.9)	(10.7)
Amortisation of original discount on subscribed capital.....	0.1	-	-
Taxation.....	1.7	0.1	2.1
<b>Other comprehensive income for the financial year, net of tax</b>	<b>(8.4)</b>	<b>(3.6)</b>	<b>(9.8)</b>
<b>Total comprehensive income for the financial year</b>	<b>(34.2)</b>	<b>5.8</b>	<b>(0.6)</b>

# STATEMENTS OF FINANCIAL POSITION

	As at 31 March		
	2017	2016	2015
	(£m)		
<b>Assets</b>			
Cash and balances with the Bank of England .....	294.8	215.4	260.8
Loans and advances to credit institutions .....	174.0	204.0	186.5
Investment securities .....	385.0	410.1	274.3
Derivative financial instruments .....	6.3	8.9	19.0
Loans and advances to customers .....	4,776.5	4,739.0	4,677.4
Deferred tax assets .....	16.4	20.4	23.9
Trade and other receivables .....	3.5	2.7	2.7
Intangible assets .....	13.3	8.2	7.0
Investment properties .....	128.9	123.7	118.6
Property, plant and equipment .....	32.1	33.9	30.2
Retirement benefit assets .....	-	0.8	-
<b>Total assets .....</b>	<b>5,830.8</b>	<b>5,767.1</b>	<b>5,600.4</b>
<b>Liabilities</b>			
Shares .....	4,427.3	4,385.1	3,988.0
Amounts due to credit institutions .....	450.3	259.0	393.3
Amounts due to other customers .....	132.7	157.0	152.4
Derivative financial instruments .....	69.0	77.1	80.8
Debt securities in issue .....	263.2	368.6	467.1
Deferred tax liabilities .....	5.0	4.7	4.5
Trade and other payables .....	10.2	15.2	12.7
Provisions for liabilities .....	3.1	2.7	2.2
Retirement benefit obligations .....	6.5	-	7.5
<b>Total liabilities .....</b>	<b>5,367.3</b>	<b>5,269.4</b>	<b>5,108.5</b>
<b>Equity</b>			
Profit participating deferred shares .....	173.0	179.5	177.1
Subscribed capital .....	75.0	74.9	74.9
General reserves .....	211.0	239.3	233.1
Revaluation reserve .....	3.5	3.4	3.4
Available for sale reserve .....	1.7	0.9	3.5
Cash flow hedging reserve .....	(0.7)	(0.3)	(0.1)
<b>Total equity attributable to members .....</b>	<b>463.5</b>	<b>497.7</b>	<b>491.9</b>
<b>Total liabilities and equity .....</b>	<b>5,830.8</b>	<b>5,767.1</b>	<b>5,600.4</b>



## SELECTED RATIOS AND OTHER FINANCIAL DATA

The following table summarises the composition of regulatory capital for the Group, under both the transitional and full implementation basis of CRD IV which is unaudited and has been derived from the Consolidated Historical Financial Statements.

	As at/financial year ended 31 March					
	2017		2016		2015	
	(£m, except percentages)					
Capital ratios	Transitional CRD IV	Full CRD IV	Transitional CRD IV	Full CRD IV	Transitional CRD IV	Full CRD IV
Common Equity Tier 1 ratio <sup>(1)</sup>	13.8%	13.8%	14.6%	14.6%	14.4%	14.4%
Total tier 1 capital ratio <sup>(1)</sup>	15.2%	13.8%	16.2%	14.6%	16.3%	14.4%
Total regulatory capital ratio <sup>(1)</sup>	16.0%	14.5%	16.9%	15.3%	16.9%	14.9%
Leverage ratio <sup>(1)</sup>	6.8%	6.2%	7.6%	6.9%	8.0%	7.0%
Liquidity coverage ratio <sup>(2)</sup>	127.0%		111.0%		-	
Other financial data						
Management expenses ratio <sup>(3)</sup>	0.86%		0.83%		0.82%	
Profit before tax (underlying) <sup>(4)</sup>	7.7		4.8		0.7	
(Loss)/Profit before tax (statutory)	(19.8)		13.5		12.4	
Net Interest Margin <sup>(4)</sup>	0.95%		1.06%		1.15%	
Underlying Net interest margin <sup>(4)</sup>	0.93%		0.90%		0.94%	

Notes:

- (1) Calculated as a percentage of risk weighted assets.
- (2) LCR measure not reported in FY ended 2015.
- (3) This 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.
- (4) The manner in which this is calculated and the rationale for presenting it are discussed in “Part VI: Presentation of Information”

For further discussion of the Society’s Common Equity Tier 1 ratio and leverage ratio, see “Part XVII: Capital Adequacy”.

## PART XVI - OPERATING AND FINANCIAL REVIEW

The following discussion should be read in conjunction with “*Part XV: Selected Financial Information*” and the Consolidated Historical Financial Statements and H1 2017/8 Interim Financial Statements incorporated by reference in this document.

The Act requires the Society 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 IFRS as adopted by the EU and applicable law. The Society’s financial year ends on 31 March each year. References in this document to **FY 2017**, **FY 2016** and **FY 2015** are to the financial year ended 31 March in each respective year.

### 1. OVERVIEW

The Society is a building society, regulated by the FCA in relation to conduct of business matters and by the PRA in relation to prudential requirements. The Society’s core business is providing personal financial services, primarily residential mortgage lending funded largely through retail savings. As a mutual organisation, other than in respect of a relatively small amount of funding provided by investors in its deferred shares (including its PIBS, its PPDS and, once issued, its CCDS), the Society is not funded by shareholders, which means that it is managed for the benefit of its members, who are its retail savings and residential mortgage customers (as well as the holders of its deferred shares), rather than for equity shareholders.

The Society 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 FY 2017, the Society invested substantially in its mortgage application and customer management systems to make it easier for members to do business and to provide operational efficiencies.

### 2. FINANCIAL PERFORMANCE

The Society’s statutory loss before tax for FY 2017 was £19.8 million (compared to a profit of £13.5 million in FY 2016 and £12.4 million in FY 2015). The driver for the reported loss 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 for FY 2017 up 60% to £7.7 million (FY 2016: £4.8 million and FY 2015: £0.7 million).

New prime residential mortgage lending for FY 2017 totalled £712 million (FY 2016: £673 million and FY 2015: £446 million) and, overall, prime owner occupied loans grew by a further 15%, as new and existing customers were supported with a competitive mortgage offering. Prime owner occupied mortgage balances grew for the fourth consecutive year, increasing by 15% to £2.3 billion (FY 2016: £2.0 billion).

The net interest margin for the FY 2017 was 0.95% (FY 2016: 1.06% and FY 2015: 1.15%). 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 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 Society’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.

Since returning to the mortgage market in FY 2013, 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, led to a £3.5 million reversal of residential provision charges in FY 2017 (FY 2016: £0.2 million increase and FY 2015: £0.8 million increase).

The Society’s total assets were maintained at £5.8 billion for the FY 2017 (FY 2016: £5.8 billion and FY 2015: £5.6 billion). This was due to lending growth offsetting the impact of running down non-core loan balances, with commercial mortgage balances falling 14% to £588 million in FY 2017 (FY 2016: £680 million and FY

2015: £835 million) of which £73 million was securitised (FY 2016: £92 million and FY 2015: £130 million) with full provision made for the residual risk to the Society.

The statutory loss for the 2017 financial year caused a reduction in the CET1 capital ratio to 13.8% (FY 2016: 14.6% and FY 2015: 14.4%). 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% (FY 2016: 7.6% and FY 2015 8.0%), the leverage ratio was significantly in excess of regulatory requirements.

### **3. IMPACT OF ECONOMIC CONDITIONS IN THE UK GENERALLY AND OUTLOOK**

As the UK negotiates its departure from the EU, there is considerable uncertainty over its future relationships within and beyond Europe. Against this backdrop, the UK is starting to see a slowdown in house price inflation and real household income growth. Early Brexit discussions have done little to alleviate market uncertainty. Following an indecisive result to the snap general election, there is a real possibility that the UK government, although currently optimistic, will be unable to negotiate a trade deal with the EU, an eventuality with, as yet, unknown consequences.

Despite the doubt enshrouding the overall economy, the residential mortgage markets appear reasonably buoyant. Whilst the TFS, launched during FY 2017, has supported the market by providing low cost four year funding, it has contributed to highly competitive mortgage pricing. Following closure of the TFS to new commitments on 28 February 2018, the markets need to adjust to the removal of this Bank of England stimulus. The Society will continue to monitor developments in this area and consider the impact on its lending and funding plans.

The non-core commercial loan book has historically proven sensitive to a downturn in the economic environment. While the Group's exposure to this sector is steadily reducing, there remains the risk of further commercial impairment provision requirements. Residential borrowers have experienced a squeeze on earnings, with inflation outstripping wage increases, and the first interest rate rise in over 10 years to 0.5% in November 2017. The markets anticipate that rates will rise further, albeit following a gradual upward trend. The Society's residential mortgage portfolios are of a high credit quality and therefore able to withstand some deterioration in economic conditions before losses are incurred. The new accounting standard IFRS 9 'Financial Instruments', applied by the Group from 1 April 2018, encapsulates a range of economic scenarios in its determination of impairment provision requirements which must be recognised on an expected, rather than incurred, loss basis. An intended consequence of IFRS 9 is that banks and building societies will recognise credit losses earlier than under current accounting standards. The Society's IFRS 9 project is progressing to timetable.

The Society recognises the ongoing need to invest in its technological capabilities. Technology is fundamental to delivering growth, excellent customer service and a robust defence against cyber risks.

Against the recent backdrop of low interest rates, political upheaval and economic uncertainty the Society has demonstrated the ability to grow its prime residential mortgage book, exit non-core activities in a controlled manner, deliver healthy and sustainable underlying profits, invest in the future and comfortably meet all regulatory capital and liquidity requirements. The Society will move forward with each of these critical objectives for the remainder of the financial year maintaining emphasis, as always, on helping more borrowers to purchase their own homes and enabling savers to prepare and plan for a secure future.

### **4. NET INTEREST INCOME**

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 net interest income but to maintain a measured level that balances continued security with long-term value for the members.

The Society's net interest income decreased by £4.7 million in FY 2017 to £55.3 million, compared to £60.0 million in FY 2016. Before one-off costs, underlying net interest income increased by £2.8 million to £54.1

million (underlying in FY 2016: £51.3 million, FY 2015: £64.7 million). 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 – see section 4 (*Recent developments*) of “Part XII: *Description of the Society's Business*” of these Listing Particulars. 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 FY 2017, as a result of not receiving the additional rate, is £6.6 million.

### Net Interest Margin

The net interest margin for FY 2017 was 0.95% (FY 2016: 1.06%, 2014/15: 1.15%). 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 TFS to promote UK lending growth.

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

#### Year to 31 March 2015 Underlying performance

	As reported £m	BTL case Impact £m	Underlying £m
Net interest income	64.7	(11.7)	53.0
Profit before tax	12.4	(11.7)	0.7
	%	%	%
Net interest margin	1.15	(0.21)	0.94

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 Society'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.

## **5. INTEREST RATE MANAGEMENT**

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, the Society 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 Act, which focus on their use to reduce risk.

The maximum level of interest rate risk is governed by the Board approved Treasury and Financial Risk Management 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 the Treasury department and reported to ALCo (as defined below).

## **6. MANAGEMENT EXPENSES**

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.

The Society's management expenses were elevated in FY 2017 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 £5.1 million to £5.7 million for FY 2017.

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 £1 million 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 £42.0 million to £44.4 million 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 FY 2017 was 0.86% (FY 2016: 0.83%, FY 2015: 0.82%).

## **7. RESULTS OF OPERATIONS FOR FY 2017, FY 2016 AND FY 2015 COMPARED**

### **7.1 Introduction**

The Society's results for FY 2017 and FY 2016 indicate a steady improvement in underlying performance, with underlying profit before tax of £7.7 million in FY 2017, £4.8 million in FY 2016, up from £0.7 million in FY 2015. The statutory (loss)/profit before tax was reported at (£19.8) million in FY 2017, £13.5 million in FY 2016 and £12.4 million in FY 2015.

The table below shows the Society's underlying profit by business division before tax in each of FY 2017, FY 2016 and FY 2015.

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

	<b>2017</b>	<b>2016</b>	<b>2015</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>
Retail	10.6	2.9	1.5
Commercial	(9.3)	(4.3)	(5.6)
Property	6.4	6.5	5.9
Intercompany adjustments	-	(0.3)	(1.1)
<b>Total Group underlying profit before tax</b>	<b>7.7</b>	<b>4.8</b>	<b>0.7</b>

Before one-off costs, underlying profitability for FY 2017 improved significantly to £7.7 million (FY 2016: £4.8 million). 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 – see section 4 (*Recent developments*) of “Part XII: *Description of the Society's Business*”. 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 FY 2017, as a result of not receiving the additional rate, is £6.6 million.

## 7.2 Total income

The Society's total income decreased to £62.4 million in FY 2017 compared to £67.2 million in FY 2016 but increased from £56.5 million in FY 2015. The following table shows the components of the Society's total income for each of FY 2017, FY 2016 and FY 2015. The figures include the additional interest on certain buy to let loans, referred to above, which was refunded in the ‘provisions for liabilities’ line of the Income Statement in FY 2017.

	<b>Financial year ended 31 March</b>		
	<b>2017</b>	<b>2016</b>	<b>2015</b>
		<i>(£m)</i>	
Interest receivable and similar income .....	108.9	126.7	136.9
Interest expense and similar charges .....	(53.6)	(66.7)	(72.2)
<b>Net interest receivable .....</b>	<b>55.3</b>	<b>60.0</b>	<b>64.7</b>
Fees and commissions receivable .....	2.7	3.7	4.2
Other operating income .....	4.1	3.9	3.8
<b>Total operating income .....</b>	<b>62.1</b>	<b>67.6</b>	<b>72.7</b>
Fair value losses on financial instruments .....	(0.2)	(1.0)	(16.3) <sup>(1)</sup>
Net realised profits.....	0.5	0.6	0.1
<b>Total income.....</b>	<b>62.4</b>	<b>67.2</b>	<b>56.5</b>

Notes:

- (1) The FY 2015 charge of £16.3m for fair value losses on financial instruments includes £11.1m relating to the hedging of commercial non-performing mortgages.

### *Net interest income*

The Society's reported net interest income decreased by £4.7 million to £55.3 million for FY 2017 compared to £60.0 million for FY 2016 and from £64.7 million in FY 2015.

### *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 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.

The table below shows interest receivable and similar income for FY 2017 and FY 2016.

	<b>FY 2017</b>	<b>FY 2016</b>
	<b>£m</b>	<b>£m</b>
On financial assets not at fair value through profit or loss:		
Loans fully secured on residential property	<b>99.2</b>	108.4
Other loans		
Loans fully secured on land	<b>21.0</b>	28.6
Investment securities	<b>5.1</b>	5.0
Other liquid assets	<b>1.0</b>	1.5
On financial assets at fair value through profit or loss:		
Net expense on derivative financial instruments	<b>(18.1)</b>	(18.2)
Loans fully secured on land	<b>0.7</b>	1.4
<b>Total interest income</b>	<b>108.9</b>	126.7
Interest receivable includes:		
Income from fixed income securities	<b>2.7</b>	3.0

Included within interest receivable and similar income is interest accrued on impaired residential mortgage assets: Group FY 2017: £1.2 million (FY 2016: £1.8 million) and interest accrued on impaired commercial mortgage assets: Group FY 2017: £4.3 million (FY 2016: £6.3 million).

The Society's interest receivable and similar income decreased by £17.8 million in FY 2017 to £108.9 million from £126.7 million in FY 2016.

### ***Interest expense and similar charges***

The Society's interest expense and similar charges decreased by £13.1 million in FY 2017 to £53.6 million from £66.7 million in FY 2016.

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

### *Other operating income*

The Society's other operating income increased by £0.2 million in FY 2017 to £4.1 million from £3.9 million in FY 2016.

	<b>FY 2017</b>	<b>FY 2016</b>
	<b>£m</b>	<b>£m</b>
Other operating income includes:		
Rent receivable on investment property	<b>6.5</b>	6.2
Operating expenses on investment property	<b>(2.3)</b>	(2.1)
Pension fund net interest	-	(0.1)
Other	<b>(0.1)</b>	(0.1)
<b>Total other operating income</b>	<b>4.1</b>	<b>3.9</b>

### *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.

The notional principal amount and fair values of derivative instruments held at FY 2017 and FY 2016 are set out below. The other derivatives held for hedging are held for economic hedging purposes but do not meet the hedge accounting criteria of IAS39 to be recorded as accounting hedges.

<b>At 31 March 2017</b>	<b>Notional principal amount 2017 £m</b>	<b>Fair values</b>	
		<b>Assets</b>	<b>Liabilities</b>
		<b>2017 £m</b>	<b>2017 £m</b>
<b>Group</b>			
<b>Derivatives held for hedging</b>			
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)
<b>Total derivative assets/(liabilities) held for hedging</b>	<b>2,247.0</b>	<b>6.3</b>	<b>(69.0)</b>

<b>At 31 March 2016</b>	<b>Notional principal amount 2016 £m</b>	<b>Fair values</b>	
		<b>Assets</b>	<b>Liabilities</b>
		<b>2016 £m</b>	<b>2016 £m</b>
<b>Group</b>			
<b>Derivatives held for hedging</b>			
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)
<b>Total derivative assets/(liabilities) held for hedging</b>	<b>2,212.7</b>	<b>8.9</b>	<b>(77.1)</b>



### 7.3 Operating expenses and similar charges

Operating expenses and similar charges (including impairment losses and provisions for liabilities) increased in FY 2017 to £87.6 million compared to £59.2 million in FY 2016 and £49.6 million in FY 2015. The increase in provisions for liabilities and charges in FY 2017 was due to the refund of additional interest that had been charged following the Court of Appeal overturning the High Court's previous decision about the Society's right to vary the interest rate on certain property investor loans – see section 4 (*Recent developments*) of "Part XII: *Description of the Society's Business*".

The table below shows the components of operating expenses and similar charges for each of FY 2017, FY 2016 and FY 2015.

	<b>FY 2017</b>	<b>FY 2016</b>	<b>FY 2015</b>
		(£m)	
Administrative expenses.....	(44.4)	(42.0)	(40.6)
Depreciation and amortisation .....	(5.7)	(5.1)	(5.4)
Impairment losses on loans and advances to customers.....	(7.6)	(8.1)	(0.2)
Provisions for liabilities and charges.....	(29.9)	(4.0)	(3.4)
<b>Total operating expenses and similar charges.....</b>	<b>(87.6)</b>	<b>(59.2)</b>	<b>(49.6)</b>

#### *Administrative expenses*

Administrative expenses increased by £2.4 million in FY 2017 to £44.4 million from £42.0 million in FY 2016, largely driven by increases in employee costs and continued investment in infrastructure and core systems to support service for members, as well as drive efficiency to manage higher business volumes.

The table below shows the components of administrative expenses for each of FY 2017, FY 2016 and FY 2015.

	<b>2017</b>	2016	2015
	£m	£m	£m
Staff costs			
Wages and salaries	<b>23.7</b>	22.6	21.9
Social security costs	<b>2.2</b>	1.8	1.9
Other pension costs	<b>1.5</b>	1.4	1.3
Rental charges payable under operating leases	<b>0.6</b>	0.5	0.6
Other administrative expenses	<b>16.4</b>	15.7	14.9
	<b>44.4</b>	42.0	40.6
Other administrative expenses include:			
Remuneration of auditor (excluding VAT element)			
Audit of these financial statements	<b>0.2</b>	0.1	0.1
Audit of the subsidiary financial statements	<b>0.1</b>	0.1	0.1
Other assurance services	<b>-</b>	0.1	-

Wages and salaries for FY 2017 include £0.1 million (FY 2016: £0.3 million, FY 2015: £0.8 million) redundancy costs paid as part of the restructuring and rationalisation of the Group's cost base.

### ***Depreciation and amortisation***

For FY 2017 depreciation and amortisation expenses increased by £0.6 million to £5.7 million as a consequence of the Head Office move that was completed in April 2016, from which point the new building, fixtures and fittings became subject to depreciation charges. For FY 2016 depreciation and amortisation expenses decreased by £0.3 million to £5.1 million.

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

The Society 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 Society 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 Society 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 Society'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.

The tables below analyse the impairment losses on loans and advances to customers for each of FY 2017 and FY 2016.

#### **FY 2017:**

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

#### FY 2016:

Group	Loans fully secured on residential property		Loans fully secured on land		Total		Total
	Individual	Collective	Individual	Collective	Individual	Collective	
	£m	£m	£m	£m	£m	£m	£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
<b>At 31 March 2016</b>	<b>11.8</b>	<b>9.0</b>	<b>34.8</b>	<b>9.1</b>	<b>46.6</b>	<b>18.1</b>	<b>64.7</b>

The high credit quality of the residential portfolios, together with the impact of house price inflation, led to a £3.5 million reversal of residential provision charges for FY 2017 (FY 2016: £0.2 million increase).

At the FY 2017 the Society had £16.3 million set aside for losses on residential mortgages (FY 2016: £20.8 million). The Society recognised commercial impairment charges of £11.1 million in FY 2017 compared with £7.9 million in FY 2016. The increase reflected changes in circumstances for certain loans and is indicative of the vulnerability of the commercial property sector to fluctuating economic conditions.

Provisions held for commercial impairment were £39.4 million for FY 2017 (FY 2016: £43.9 million), equivalent to 6.7% of the current loan book (FY 2016: 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 (31 March 2016: 46%).

During the 2017 financial year there were impairment credits of £0.3 million (FY 2016: charges of £0.1 million) against loans in structured entities, Sandwell Commercial Finance No.1 Plc: £0.2 million credit (FY 2016: £0.6 million charge) and Sandwell Commercial Finance No. 2 Plc: £0.1 million credit (FY 2016: £0.5 million 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 £1.8 million (FY 2016:

£4.2 million) against loans in structured entities, Sandwell Commercial Finance No.1 Plc: £nil (FY 2016: £2.4 million) and Sandwell Commercial Finance No. 2 Plc: £1.8 million (FY 2016: £1.8 million). The carrying value of the external loan notes has been adjusted by an equivalent amount.

#### ***Impairment losses/(recoveries) on investment securities***

During FY 2017 and FY 2016 none of the Society's treasury investments were either past due or impaired and no impairment charges were required during the year.

#### ***Provisions for liabilities***

The table below shows the components of provisions for liabilities and charges for each of FY 2017 and FY 2016.

	<b>Buy to let</b>	<b>FSCS</b>	<b>Onerous contracts</b>	<b>Other</b>	<b>Total</b>
	<b>2017</b>	<b>2017</b>	<b>2017</b>	<b>2017</b>	<b>2017</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
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
<b>At end of year</b>	<b>-</b>	<b>0.8</b>	<b>-</b>	<b>2.3</b>	<b>3.1</b>

	<b>Buy to let</b>	<b>FSCS</b>	<b>Onerous contracts</b>	<b>Other</b>	<b>Total</b>
	<b>2016</b>	<b>2016</b>	<b>2016</b>	<b>2016</b>	<b>2016</b>
	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>
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
<b>At end of year</b>	<b>-</b>	<b>1.4</b>	<b>0.1</b>	<b>1.2</b>	<b>2.7</b>

#### ***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 FY 2017, 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 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 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, the 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.

## **7.4 Profit before tax**

Reflecting the above factors, the Society's statutory loss before tax was £19.8 million in FY 2017, £13.5 million profit in FY 2016 and £12.4 million profit in FY 2015. Excluding one-off charges, the Society's underlying profit before tax was £7.7 million in FY 2017, £4.8 million in FY 2016 and £0.7 million in FY 2015.

## **7.5 Taxation**

The tax charge for FY 2017 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 Society's ability to vary the interest rate applicable to certain buy to let loans.

	<b>2017</b>	<b>2016</b>
	<b>£m</b>	<b>£m</b>
UK corporation tax at 20% (FY 2016: 20%)	<b>0.9</b>	2.5
Corporation tax - adjustment in respect of prior years	-	(1.2)
Total current tax	<b>0.9</b>	1.3
Deferred tax		
Current year	<b>5.6</b>	1.8
Adjustment in respect of prior periods	<b>(0.5)</b>	1.0
<b>Tax on (loss)/profit on ordinary activities</b>	<b>6.0</b>	4.1

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

	<b>2017</b>	<b>2016</b>
	<b>£m</b>	<b>£m</b>
(Loss)/Profit before tax	<b>(19.8)</b>	13.5
(Loss)/Profit before tax multiplied by the UK standard rate of tax of 20% (FY 2016: 20%)	<b>(4.0)</b>	2.7
Effects of:		
Income not taxable and expenses not deductible for tax purposes	<b>2.2</b>	0.7
Changes to tax rate	<b>0.1</b>	1.4
Adjustment in respect of prior years	<b>(0.5)</b>	(0.2)
Transfer pricing adjustments	-	-
Write down of deferred tax assets	<b>9.2</b>	-
Revaluation	<b>(1.0)</b>	(0.5)
<b>Tax charge</b>	<b>6.0</b>	4.1

## 7.6 Comprehensive income

The table below shows a summary of the Society's statement of comprehensive income for FY 2017 and FY 2016.

	Financial year ended 31 March	
	2017	2016
	(£m)	
<b>(Loss)/Profit for the financial year</b>	<b>(25.8)</b>	<b>9.4</b>
<b>Other comprehensive income</b>		
<b>Items that may subsequently be reclassified to profit or loss</b>		
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	0.1	0.2
<b>Items that will not subsequently be reclassified to profit or loss</b>		
Gains on revaluation of land and buildings	0.6	-
Actuarial losses on defined benefit obligations	(10.4)	(0.9)
Amortisation of original discount on subscribed capital	0.1	-
Taxation	1.7	0.1
<b>Other comprehensive income for the financial year, net of tax</b>	<b>(8.4)</b>	<b>(3.6)</b>
<b>Total comprehensive income for the financial year</b>	<b>(34.2)</b>	<b>5.8</b>

The Society's total comprehensive income in FY 2017 was (£34.2 million) compared to £5.8 million in FY 2016 and (£0.6 million) in FY 2015.

## 8. SEGMENTAL ANALYSIS

Operating segments are reported in accordance with the internal management 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 Society 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.

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 Society'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 tables below show Society's segmental results for each of FY 2017 and FY 2016.

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)
<b>Net interest receivable/(expense)</b>	<b>54.8</b>	<b>3.4</b>	<b>(2.9)</b>	<b>-</b>	<b>55.3</b>
Fees and commissions receivable	2.7	-	-	-	2.7
Other operating income	37.5	-	4.1	(37.5)	4.1
<b>Total operating income</b>	<b>95.0</b>	<b>3.4</b>	<b>1.2</b>	<b>(37.5)</b>	<b>62.1</b>
Fair value (losses)/gains on financial instruments	(0.3)	0.1	-	-	(0.2)
Net realised gains	0.5	-	-	-	0.5
<b>Total income</b>	<b>95.2</b>	<b>3.5</b>	<b>1.2</b>	<b>(37.5)</b>	<b>62.4</b>
Administrative expenses	(42.5)	(1.7)	(0.2)	-	(44.4)
Depreciation and amortisation	(5.7)	-	-	-	(5.7)
<b>Operating profit before revaluation gains, impairment and provisions</b>	<b>47.0</b>	<b>1.8</b>	<b>1.0</b>	<b>(37.5)</b>	<b>12.3</b>
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)
<b>(Loss)/Profit before tax</b>	<b>(16.9)</b>	<b>(9.3)</b>	<b>6.4</b>	<b>-</b>	<b>(19.8)</b>

Statements of Financial Position At 31 March 2017	Retail £m	Commercial £m	Property £m	Consolidation adjustments £m	Total Group £m
<b>Total assets</b>	<b>5,744.3</b>	<b>548.8</b>	<b>132.1</b>	<b>(594.4)</b>	<b>5,830.8</b>
<b>Total liabilities</b>	<b>5,295.2</b>	<b>588.6</b>	<b>125.8</b>	<b>(642.3)</b>	<b>5,367.3</b>
<b>Capital expenditure</b>	<b>9.0</b>	<b>-</b>	<b>-</b>	<b>-</b>	<b>9.0</b>

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)
<b>Net interest receivable/(expense)</b>	<b>58.2</b>	<b>4.7</b>	<b>(2.9)</b>	<b>-</b>	<b>60.0</b>
Fees and commissions receivable	3.7	-	-	-	3.7
Other operating income	30.5	-	4.1	(30.7)	3.9
<b>Total operating income</b>	<b>92.4</b>	<b>4.7</b>	<b>1.2</b>	<b>(30.7)</b>	<b>67.6</b>
Fair value (losses)/gains on financial instruments	(1.2)	0.6	-	(0.4)	(1.0)
Net realised gains	0.6	-	-	-	0.6
<b>Total income</b>	<b>91.8</b>	<b>5.3</b>	<b>1.2</b>	<b>(31.1)</b>	<b>67.2</b>
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)
<b>Profit/(Loss) before tax</b>	<b>11.6</b>	<b>(4.3)</b>	<b>6.5</b>	<b>(0.3)</b>	<b>13.5</b>

<b>Statements of Financial Position*</b>	<b>Retail</b>	<b>Commercial</b>	<b>Property</b>	<b>Consolidation</b>	<b>Total</b>
<b>At 31 March 2016</b>	<b>£m</b>	<b>£m</b>	<b>£m</b>	<b>adjustments</b>	<b>Group</b>
				<b>£m</b>	<b>£m</b>
<b>Total assets</b>	5,656.6	643.2	128.1	(660.8)	5,767.1
<b>Total liabilities</b>	5,183.1	662.2	90.3	(666.2)	5,269.4
<b>Capital expenditure</b>	10.0	-	-	-	10.0

\* Prior year comparatives have been restated to remove intra-divisional netting with a matching movement in consolidation adjustments.

### Retail reporting segment

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 in 2016/17 improved with an underlying profit before tax of £10.6 million (FY 2016: £2.9 million). A 15% growth in prime residential mortgage balances, as a result of completions of £712 million (FY 2016: £673 million), made a positive contribution to the segment result as did a £3.5 million reduction (FY 2016: £0.2 million 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 2017 financial year (FY 2016: 1.27%).

### Commercial reporting segment

Commercial lending is a non-core activity and the Society 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 FY 2017, impairment charges rose to £11.1 million, compared with £7.9 million in FY 2016. This led to a decline in segment performance and an underlying loss before tax of £9.3 million (FY 2016: £4.3 million).

The overall exposure to assets secured on commercial properties had fallen from £1.7 billion in 2007/8 to £0.6 billion at 31 March 2017. £73 million of these balances are securitised (FY 2016: £92 million).

### Property reporting segment

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 £5.4 million has been reported for FY 2017 for the West Bromwich Homes Limited residential property portfolio (FY 2016: £5.5 million), as a result of house price inflation during the year. The carrying value of the portfolio at 31 March 2017 was £128.9 million (FY 2016: £123.7 million). One property was sold during the year achieving its book value of £0.2 million. Consistent with the prior period, the investment properties generated a trading net income of £1.0 million.



## LIQUIDITY AND FUNDING

### 8.1 Overview

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

### 8.2 Analysis of cash flows

The table below summarises the Society's statement of cash flows for FY 2017 and FY 2016.

	2017 £m	2016 £m
<b>Net cash inflow/(outflow) from operating activities (below)</b>	<b>138.7</b>	<b>220.3</b>
<b>Cash flows from investing activities</b>		
Purchase of investment securities	(230.4)	(386.7)
Proceeds from disposal of investment securities	213.1	298.0
Proceeds from disposal of investment properties	0.2	0.4
Purchase of property, plant and equipment and intangible assets	(9.6)	(8.8)
Proceeds from disposal of property, plant and equipment	0.5	-
New funding to subsidiaries	-	-
Dividends received	-	-
Repayment of funding from subsidiaries	-	-
<b>Net cash flows from investing activities</b>	<b>(26.2)</b>	<b>(97.1)</b>
<b>Cash flows from financing activities</b>		
Repayment of mortgage backed loan notes	(106.0)	(98.5)
<b>Net cash flows from financing activities</b>	<b>(106.0)</b>	<b>(98.5)</b>
Net increase in cash	6.5	24.7
Cash and cash equivalents at beginning of year	468.8	444.1
<b>Cash and cash equivalents at end of year</b>	<b>475.3</b>	<b>468.8</b>

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

	2017 £m	2016 £m
Cash in hand (including Bank of England Reserve account)	287.6	208.7
Loans and advances to credit institutions	174.0	204.0
Investment securities	13.7	56.1
	<b>475.3</b>	<b>468.8</b>

The Group is required to maintain certain mandatory balances with the Bank of England which, at 31 March 2017, amounted to £7.2 million (FY 2016: £6.7 million). The movement in these balances is included within cash flows from operating activities.

	2017 £m	2016 £m
<b>Cash flows from operating activities</b>		
(Loss)/Profit on ordinary activities before tax from continuing activities	(19.8)	13.5
Movement in prepayments and accrued income	(0.8)	(0.2)
Movement in accruals and deferred income	(2.6)	(0.4)
Impairment on loans and advances	7.6	8.1
Depreciation and amortisation	5.7	5.1
Revaluations of investment properties	(5.4)	(5.5)
Movement in provisions for liabilities	0.4	0.5
Movement in derivative financial instruments	(5.5)	6.4
Movement in fair value adjustments	(0.7)	(2.3)
Movement in subscribed capital	0.1	-

	2017 £m	2016 £m
<b>Cash flows from operating activities</b>		
Change in retirement benefit obligations	(3.1)	(9.2)
<b>Cash flows from operating activities before changes in operating assets and liabilities</b>	<b>(24.1)</b>	16.0
Movement in loans and advances to customers	(47.7)	(72.4)
Movement in loans and advances to credit institutions	(0.5)	0.6
Movement in shares	45.7	407.1
Movement in deposits and other borrowings	167.0	(129.7)
Movement in trade and other receivables	-	2.4
Movement in trade and other payables	(1.7)	(3.7)
<b>Net cash inflow/(outflow) from operating activities</b>	<b>138.7</b>	220.3

### 8.3 Liquidity

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;
- LCR - high quality liquid assets as a proportion of stressed cash outflows over the next 30 days; and
- NSFR - the ratio of available stable funding to required stable funding, representing a longer term liquidity measure than the LCR.
- 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 £57 million of gilts, obtained under an asset swap agreement, which are not included in Group liquidity but do qualify as buffer liquidity for regulatory purposes (FY 2016: £137 million treasury bills obtained under the Funding for Lending Scheme).

As at 31 March 2017 the Society's liquidity holdings comprised solely high quality liquid assets with 100% of treasury investments rated single A or better or held with a Global Systemically Important Counterparty (FY 2016: 100%). The Society 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. There was no impairment provision requirement for treasury assets at 31 March 2017 (FY 2016: nil).

### 8.4 Funding strategy

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 relatively stable low level.

## ***Retail***

Aligned to the principles of mutuality, the Society is primarily funded by retail deposits, with residential mortgage assets for FY 2017 amply covered 1.04 times (FY 2016: 1.06 times) by retail savings balances. The retail savings book marginally increased in FY 2017 to £4.43 billion (FY 2016: £4.39 billion, FY 2015: £3.99 billion), with 60% (FY 2016: 59%) held in branch-based accounts.

## ***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 TFS. The Society, along with other financial institutions, has taken advantage of this opportunity to obtain low cost term funding.

### **8.5 Managing liquidity and funding 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. For further information regarding the Society's liquidity risk management, see "*Part XIX Risk Management – Liquidity Risk*".

## ***External credit ratings***

The Society withdrew from the ratings process in 2012. Moody's however maintain a non-participating rating as outlined below:

	<u>Long-term</u>	<u>Short-term</u>
Moody's (positive) .....	B1	NP

### **8.6 Treasury assets**

#### ***Liquidity and investment portfolio***

The portfolio's liquid assets comprise cash held at central banks, highly rated debt securities issued by a limited range of government and multi-lateral development banks (referred to as supranationals). In addition, the portfolio comprises highly rated liquid assets (covered bonds, RMBS and asset-backed securities) that are eligible for accessing central bank funding operations. The other securities are available for sale investment securities. Movements in the portfolio reflect legacy asset disposals, market prices and the Society's operational and strategic liquidity requirements.

Liquid asset balances for FY 2017 were a little higher than the prior year at £854 million (FY 2016: £830 million). The Society's 'on balance sheet' liquidity ratio was 17.0% (FY 2016: 17.3%).

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

**At 31 March 2017** Liquidity portfolio

	£m	%
<b>Buffer liquidity</b>		
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
<b>Total buffer liquidity</b>	<b>626.7</b>	<b>73.4</b>
Other securities - rated single A or better	45.8	5.4
Subsidiary/other liquidity	181.3	21.2
<b>Total liquidity</b>	<b>853.8</b>	<b>100.0</b>

**At 31 March 2016** Liquidity portfolio

	£m	%
<b>Buffer liquidity</b>		
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
<b>Total buffer liquidity</b>	<b>495.6</b>	<b>59.7</b>
Other securities - rated single A or better	123.2	14.9
Subsidiary/other liquidity	210.7	25.4
<b>Total liquidity</b>	<b>829.5</b>	<b>100.0</b>

In addition to the above Buffer Liquidity, the Society also holds £nil of FLS treasury bills (2016: £137 million) and £57 million of Gilts obtained through an asset swap (2016: £nil) that it includes in its regulatory calculations, which are not included in Group Liquidity.

The Society 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 Society.

The Society 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 Society 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 Society's treasury investments were either past due or impaired and no impairment charges were required during the year.

At 31 March 2017, 100.0% (FY 2016: 100.0%) of the Society'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 Society 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 Society's treasury investment portfolio, all of which are denominated in sterling:

	2017 £m	2016 £m
<b>Concentration by credit grading</b>		
AAA	344.2	286.9
AA+ to AA-	412.0	353.9
A+ to A-	76.1	166.1
BBB+	21.5	21.6
Building societies	-	1.0

	2017 £m	2016 £m
Other	-	-
	<b>853.8</b>	<b>829.5</b>
<b>Concentration by sector</b>		
Financial institutions	219.9	327.2
Asset backed securities	249.4	233.4
Supranational institutions	89.7	53.5
Sovereign	294.8	215.4
	<b>853.8</b>	<b>829.5</b>
<b>Concentration by region</b>		
UK	669.8	626.6
Europe (excluding UK)	72.5	86.3
North America	7.2	32.9
Australasia	13.2	28.8
Supranational	89.7	53.5
Asia	1.4	1.4
	<b>853.8</b>	<b>829.5</b>

All assets shown above, other than cash and loans and advances to banks, are classified as available-for-sale investment securities.

#### ***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.

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 2017 and 2016 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
	<b>1,204.4</b>	<b>4,626.4</b>	<b>1,039.2</b>	<b>4,727.9</b>

In addition to the above, at 31 March 2017, Group loans and advances to credit institutions included £82.6 million (FY 2016: £81.5 million) of collateral pledged against derivative financial instruments and £1.4 million (FY 2016: £1.4 million) cash collateral paid in relation to sale and repurchase agreements.

## **9. LENDING AND CAPITAL ADEQUACY**

For an analysis of the Society's lending portfolios, see "*Part XVIII: Selected Statistical Information*".

For an analysis of the Society's capital adequacy, see "*Part XVII: Capital Adequacy*"

## **10. CONTRACTUAL COMMITMENTS**

For details of the amounts of certain of the Society's financial and other contractual liabilities and when payments are due, without taking into account customer deposits, deposits by other financial institutions and debt securities in issue and derivative financial instruments, see the 2017 Financial Statements incorporated by reference in this document.

## **11. OFF BALANCE SHEET ARRANGEMENTS**

For a description of the Society's off-balance sheet commitment items under IFRS, see the 2017 Financial Statements incorporated by reference in this document.

## **12. RELATED PARTY TRANSACTIONS**

For a description of the Society's related party transactions, see note 36 to the 2017 Financial Statements incorporated by reference in this document.

## **13. ACCOUNTING POLICIES AND JUDGEMENTS IN APPLYING ACCOUNTING POLICIES AND CRITICAL ACCOUNTING ESTIMATES**

For details on the Society's accounting policies under IFRS and its judgements in applying the accounting policies and critical accounting estimates, see notes 1 and 2 to the 2017 Financial Statements incorporated by reference herein.

### **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. See "*Part I: Risk Factors - Changes in accounting policies or standards*".

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.

## **14. DISCLOSURES ABOUT RISK**

For a discussion of the Society's risk management activities, see "*Part XIX: Risk Management*".

## PART XVII - CAPITAL ADEQUACY

### OVERVIEW

Capital is held by the Society to protect its depositors, to cover its inherent risks, to provide a cushion for stress events and to support its business strategy. The following tables set out selected consolidated information which has been derived from the Consolidated Historical Financial Statements, including Pillar 3 disclosures for the years ended 31 March 2017, 31 March 2016 and 31 March 2015.

### TOTAL AVAILABLE CAPITAL

The table below summarises the composition of regulatory capital for the Group, under both the transitional and full implementation basis of CRD IV. During the years ended 31 March 2017 and 31 March 2016, the individual entities within the Group and the Group itself complied with all of the externally imposed capital requirements.

At 31 March 2017	Transitional CRD IV rules	Full implementation of CRD IV	Transitional CRD IV rules	Full implementation of CRD IV	Transitional CRD IV rules	Full implementation of CRD IV
	2017 £m	2017 £m	2016 £m	2016 £m	2015 £m	2015 £m
<b>Common Equity Tier 1 capital</b>						
General reserves	211.0	211.0	239.3	239.3	233.1	233.1
Revaluation reserve <sup>(1)</sup>	3.5	3.5	3.4	3.4	3.4	3.4
Available for sale reserve (AFS)	1.7	1.7	0.9	0.9	3.5	3.5
Cash flow hedging reserve	(0.7)	(0.7)	(0.3)	(0.3)	(0.1)	(0.1)
Profit participating deferred shares <sup>(2)</sup>	173.0	173.0	179.5	179.5	177.1	177.1
<b>Common Equity Tier 1 prior to regulatory adjustments</b>	<b>388.5</b>	<b>388.5</b>	<b>422.8</b>	<b>422.8</b>	<b>417.0</b>	<b>417.0</b>
<i>Regulatory adjustments:</i>						
Defined benefit pension fund asset <sup>(3)</sup>	-	-	(0.8)	(0.8)	-	-
Cash flow hedging reserve <sup>(4)</sup>	0.7	0.7	0.3	0.3	0.1	0.1
Intangible assets and goodwill <sup>(5)</sup>	(13.3)	(13.3)	(8.2)	(8.2)	(7.0)	(7.0)
Deferred tax asset relating to operating losses <sup>(6)</sup>	(8.9)	(8.9)	(14.7)	(14.7)	(15.7)	(15.7)
Other adjustments <sup>(7)</sup>	1.0	1.0	(2.4)	(2.4)	(4.1)	(4.1)
<b>Common Equity Tier 1 capital</b>	<b>368.0</b>	<b>368.0</b>	<b>397.0</b>	<b>397.0</b>	<b>390.3</b>	<b>390.3</b>
<b>Additional Tier 1 capital</b>						
Permanent interest bearing shares (PIBS)	75.0	75.0	74.9	74.9	74.9	74.9
<i>Regulatory adjustments:</i>						
Amortisation of PIBS under transitional rules <sup>(8)</sup>	(37.5)	(75.0)	(30.0)	(74.9)	(22.5)	(74.9)
<b>Total Tier 1 capital</b>	<b>405.5</b>	<b>368.0</b>	<b>441.9</b>	<b>397.0</b>	<b>442.7</b>	<b>390.3</b>
<b>Tier 2 capital</b>						
Collective provision	22.1	22.1	18.1	18.1	16.6	16.6
Contingency against collective provision add-back <sup>(9)</sup>	(2.5)	(2.5)	-	-	(0.5)	(0.5)
<b>Total capital</b>	<b>425.1</b>	<b>387.6</b>	<b>460.0</b>	<b>415.1</b>	<b>458.8</b>	<b>406.4</b>

- (1) Revaluation reserve relates to the increase in value of the land and buildings owned by the Group and held for use by the business.
- (2) PPDS are a form of CET1 capital for building societies which are unsecured deferred shares and rank behind the claims of all subordinated noteholders, depositors, creditors and investing members of the Society including PIBS. The 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 cumulative reserves are in deficit.
- (3) Under CRD IV defined benefit pension fund assets are deducted from capital.



- (4) The cash flow hedging reserve is not included in capital.
- (5) Intangible assets include capitalised software and goodwill. A full deduction is made from CET1 for intangible assets and goodwill.
- (6) Under the rules of CRD IV (transitional and on full implementation) deferred tax assets relating to previous operating losses are deducted from capital.
- (7) Other adjustments comprise deductions for additional valuation adjustments of £0.5 million (2016: £nil, 2015: £nil) and low quality mortgage backed security notes of £0.5 million (2016: £2.4 million, 2015: £4.1 million) together with an adjustment to add back the accumulated loss within the risk remote securitisations that was deducted from the Group's accounting reserves of £2.1 million (2016: £nil, 2015: £nil).
- (8) PIBS are unsecured deferred shares and in a winding up or dissolution of the Society, rank behind the claims of all subordinated noteholders, depositors, creditors and investing members of the Society but ahead of PPDS. The holders of PIBS are not entitled to any share in any final surplus upon winding up or dissolution of the Society. Under the transitional rules applicable to the 2017 financial year, 50% (2016: 40%, 2015: 30%) of the value of PIBS is deducted from tier 1 capital. Under the transitional rules the amortisation deduction is increased by 10% per annum every 1 January through to 2021, with the final 10% deducted on 5 April 2021, the earliest call date for the PIBS.
- (9) The Tier 2 capital comprises the Society's collective impairment provisions. The contingency against collective provision add back is an allowance for part of the collective provision which has some specific characteristics and which has therefore been disallowed for capital purposes.

## CAPITAL MANAGEMENT AND REPORTING

Capital is held to provide a cushion to absorb losses that may occur during the economic cycle. In assessing the adequacy of its capital, the Group considers its risk appetite, the material risks to which the Group is exposed and the appropriate management strategies for each of the Group's material risks, including whether or not capital provides an appropriate mitigant.

The Group considers its overall capital requirement as part of its Internal Capital Adequacy Assessment Process (ICAAP).

The regulatory capital adequacy of the Solo consolidation and the Consolidation Group are reported to the Regulator quarterly. In addition, Group capital requirements are reviewed on a monthly basis and the results of this monitoring are reported to the Group Capital Committee (GCC), Risk Committee (RC) and the Board.

### Pillar 2

Pillar 2 covers risks not fully covered by Pillar 1 or those risks outside the scope of Pillar 1 referred to as Pillar 2A; and risks to which the Society may become exposed over a forward-looking planning horizon (e.g. due to changes in the economic environment) referred to as Pillar 2B. The Pillar 2A requirement is therefore a 'point in time' assessment whereas the Pillar 2B requirement is forward-looking.

### *Internal Capital Adequacy Assessment Process (ICAAP)*

On an annual basis the Group conducts an ICAAP covering all risks. This is used to assess the Group'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 through the ICAAP and is approved by the Board. The ICAAP 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. An allocation of capital is made for each of the following risks facing the Society:

- Credit risk from mortgages and other retail lending;
- Credit risk from treasury assets and derivatives;
- Concentration risk (which can exacerbate credit exposures);
- Market risk;
- Residential property holding risk;
- Interest rate risk;
- Basis risk;
- Operational risk; and
- Pension liability risk.

This allocation is based on regulatory requirements for credit risk and operational risk (Pillar 1) with additional allocations to reflect the degree of residual risk that remains after allowing for the effect of the risk controls

operated by the Society (Pillar 2A). The Pillar 2A allocation of capital is a point in time assessment which reflects risks that are not captured or not adequately captured in Pillar 1.

A further capital allocation is made for Pillar 2B. This is a forward-looking assessment, which examines the Society's business plans and subjects them to economic and operational stresses over a five year planning horizon. The severity and duration of the stress scenarios used is determined by reference to a severe stress scenario published by the PRA. In addition, the Society incorporates additional second order stresses to make the capital stress even more severe than that prescribed by the regulator. This includes allowance for operational stresses and, allowance for significant increases in retail funding costs.

The output from the assessment of Pillar 1, 2A and 2B capital requirements is reviewed by the GCC and RC prior to the finalisation of the ICAAP and submission to the Board for formal approval as part of the corporate planning process. The Society continues to be strongly capitalised and maintains its capital substantially above current regulatory requirements.

The ICAAP is used by the PRA in its Supervisory Review and Evaluation Process through which it sets the Society's capital requirements. The PRA also considers whether a PRA Buffer is required. The **PRA Buffer** is an amount of capital that firms should hold, in addition to their individual capital guidance, to cover losses that may arise under a severe stress scenario (Pillar 2B) after allowance for the CRD IV buffer (see below).

## PILLAR 2B - CRD IV CAPITAL BUFFERS

To promote the conservation of capital and the build-up of adequate buffers that can be drawn down in periods of stress, CRD IV requires the holding of supplementary common equity tier 1 capital buffers from 1 January 2016, known as Pillar 2B. These comprise a Capital Conservation Buffer and a macro-prudential countercyclical buffer. To the extent that the PRA considers these CRD IV buffers to be insufficient a PRA Buffer will be added to the Society's capital requirement although the PRA has stated that it believes that for most firms, most of the time, the CRD IV buffers are likely to be sufficient once fully phased in.

## MINIMUM CAPITAL REQUIREMENT - PILLAR 1

Under the regulator's rules, a minimum level of capital (Pillar 1) must be held for credit risk, operational risk and market risk. The Group has adopted the Standardised Approach to calculate the minimum regulatory capital requirement for credit risk and operational risk. The table below shows the Group's overall minimum capital requirement for credit, operational and market risk.

The following table shows the average risk weights applied by the Society as at 31 March 2017 and 2016. The credit risk requirement has been calculated under the Standardised Approach (expressed as 8% of the risk weighted exposure amounts for each of the applicable standardised credit risk exposure classes). Details of the Standardised Approach to the calculation of regulatory requirements are contained in CRD IV.

	2017 Average risk weights	2017	2016 Average risk weights	2016	2015 Average risk weights	2015
Credit risk	%	£m	%	£m	%	£m
Residential mortgage loans (performing)	35.4	119.4	35.7	116.2	35.8	110.1
Commercial mortgage loans (performing)	98.9	9.7	97.7	15.2	97.2	24.1
Residential mortgage loans (past due)	103.0	8.1	102.1	9.4	102.1	11.6
Commercial mortgage loans (past due)	146.1	42.6	146.1	43.0	145.9	43.0
Liquidity (Treasury instruments and cash)	11.9	7.7	15.7	9.7	12.8	7.3
Other items	100.0	14.1	104.8	14.1	102.6	13.1
Total capital requirements – credit risk		201.6		207.6		209.2
Operational risk - Standardised Approach		7.7		7.6		6.7
Market and counterparty credit risk*		3.8		2.4		1.6
Total Pillar 1 capital requirement		213.1		217.6		217.5

	2017 Average risk weights	2017	2016 Average risk weights	2016	2015 Average risk weights	2015
<b>Credit risk</b>	%	£m	%	£m	%	£m
Total capital available under transitional CRD IV rules		425.1		460.0		458.8
Excess of capital over minimum capital requirement under Pillar 1		212.0		242.4		241.3

\* Market and counterparty credit risk above includes potential market value losses on OTC derivatives, known as Credit Valuation Adjustment (CVA). The CVA charge has been calculated based on the net contractual collateral derivative position of the Society (also includes potential future credit exposures relating to derivatives and haircut re Secured Financing Transactions (Repos)).

## QUALITY OF CAPITAL

CRD IV introduced more stringent requirements for the eligibility of capital instruments with a focus on Common Equity Tier 1 as the principal component of regulatory tier 1 capital, and changes to the regulatory deductions from Common Equity Tier 1. The regulations set a minimum of tier 1 capital at 6% of RWAs, of which CET1 is required to be a minimum of 4.5% of RWAs. The total of tier 1 and Tier 2 capital must be a minimum of 8% of RWAs.

The following table shows the Society's capital ratios as at 31 March 2017, 2016 and 2015 on a transitional and full implementation basis:

	Transitional CRD IV rules 2017 %	Full implementation of CRD IV 2017 %	Transitional CRD IV rules 2016 %	Full implementation of CRD IV 2016 %	Transitional CRD IV rules 2015 %	Full implementation of CRD IV 2015 %
<b>Common Equity Tier 1</b>	13.8	13.8	14.6	14.6	14.4	14.4
<b>Tier 1</b>	15.2	13.8	16.2	14.6	16.3	14.4
<b>Total capital</b>	16.0	14.5	16.9	15.3	16.9	14.9

CRD IV applies the principle that tier 1 capital is available to absorb losses of the business on a 'going concern' basis. The Society's PIBS do not contain a mechanism allowing for principal loss absorption on a going concern basis, and therefore do not meet the necessary requirements for tier 1 capital under CRD IV. The PIBS are, therefore, 'grandfathered' and recognised as additional tier 1 capital on an amortising basis.

The statutory loss for the financial year caused a reduction in the CET1 capital ratio which fell to 13.8% as at 31 March 2017 (31 March 2016: 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% as at 31 March 2017 (31 March 2016: 7.6%), the Society's leverage ratio remains significantly in excess of regulatory requirements.

## Modernisation of the Society's Capital Structure

In February 2017, the Society announced that it was seeking clarification from the EBA in relation to the eligibility of its PPDS as CET1 capital, following an investor challenge.

While the Society continues to believe that the PPDS met the CET1 criteria in all respects, the Society in the meantime had constructive engagement with major holders of both the PPDS and the PIBS with respect to its options. It was clear throughout discussions with these major holders that, irrespective of the outcome of the EBA's deliberations on eligibility of the PPDS, the major holders and the Society were aligned in their views that a modernisation of the Society's capital structure would be appropriate. Following these discussions, the Society announced on 13 December 2017 its plans to conduct the LME involving its PPDS and the PIBS.

The Society launched the LME on 8 March 2018, and announced the final results of the LME on 10 April 2018. The Society expects the LME to settle on 12 April 2018.

In the December Announcement, the Society noted that on an indicative basis only, had the LME been successfully completed on 30 September 2017 (the latest reporting date of the Society prior to the December Announcement) and assuming only those PIBS holders from whom binding commitments have been received by the Society participated in the LME, the Society expected that its CET1 ratio would have decreased by approximately 0.4 percentage points to 13.7 per cent., its total capital ratio (with full impact of CRD IV implementation) would have increased by approximately 0.4 percentage points to 15.2 per cent. and Member Reserves would have increased by approximately £42 million. On the same basis but assuming that 100 per cent. of PIBS holders participated in the LME, the Society expected that its CET1 ratio would have increased by approximately 0.3 percentage points to 14.4 per cent., its total capital ratio (with full impact of CRD IV implementation) would have increased by approximately 1.1 percentage points to 15.9 per cent. and Member Reserves would have increased by approximately £52 million.

The offer period for the LME expired on 5 April 2018, and the LME is scheduled to settle on 12 April 2018. Based on the results of the LME announced in the Results Announcement on 10 April 2018, on an indicative basis only, had the LME been successfully completed on 30 September 2017 the Society expects that its CET1 ratio would have been maintained at 14.1 per cent., its total capital ratio (with full impact of CRD IV implementation) would have increased by approximately 1 percentage point to 15.8 per cent. and Member Reserves would have increased by approximately £50 million, before any accounting adjustment to other reserves to reflect the fair values of the new instruments.

On 19 January 2018, the Society, having received the requisite consents of the holders of more than three-quarters of the PPDS, made certain variations to the Special Conditions of Issue of the PPDS to address the investor challenges raised with respect to the PPDS. Accordingly, the Society elected to withdraw its request for clarification from the EBA. The Directors consider that the Society will continue to remain adequately capitalised.

## LEVERAGE

CRD IV introduced a non-risk based leverage ratio that is supplementary to the risk based capital requirements and is intended as a ‘backstop’ measure. The calculation determines a ratio based on the relationship between tier 1 capital and total balance sheet exposures. The leverage ratio does not distinguish between unsecured and secured loans or recognise the ratio of loan to collateral value of secured lending. The CRD IV requirement is for the minimum level of this ratio to be 3.25%. For the Society this measure does not come into effect until 2018.

The following table shows the Society’s leverage ratios, on a transitional and full CRD IV implementation basis, as at 31 March 2017, 2016 and 2015:

	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	Transitional CRD IV rules 2015 £m	Full implementation of CRD IV 2015 £m
Total Tier 1 capital	405.5	368.0	441.9	397.0	442.7	390.3
Total assets per the Statement of Financial Position	5,830.8	5,830.8	5,767.1	5,767.1	5,600.4	5,600.4
Mortgage pipeline and committed facilities	72.1	72.1	79.7	79.7	49.3	49.3
Common Equity adjustments relating to assets	(20.5)	(20.5)	(26.1)	(26.1)	(26.8)	(26.8)

	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	Transitional CRD IV rules 2015 £m	Full implementation of CRD IV 2015 £m
Repurchase agreements and Potential Future Credit Exposure for swaps	91.8	91.8	38.5	38.5	65.7	65.7
Netted derivative adjustment	(37.9)	(37.9)	(70.0)	(70.0)	(22.3)	(22.3)
Adjusted assets	5,936.3	5,936.3	5,789.2	5,789.2	5,540.8	5,540.8
Leverage ratio (%)	6.8	6.2	7.6	6.9	8.0	7.0

At 31 March 2017 the leverage ratio of the Society was significantly above the 3.25% regulatory minimum. Under the transitional CRD IV provisions it was at 6.8% (31 March 2016: 7.6%). Upon full implementation this will reduce to 6.2% (2016: 6.9%). The Society anticipates that there has been little change in the ratio during FY 2017, although asset quality continues to improve as high quality prime new residential lending assets replace commercial assets as they redeem. In considering a target for this ratio the Society recognises the importance of continuing to originate high quality assets even though this will have the effect of diluting the current leverage ratio.

## RWA FLOW STATEMENT

The following table shows the movement in credit risk RWAs over the year to 31 March 2017. Movements reflect changes in book size and book quality.

	Residential Mortgages £m	Commercial Mortgages £m	Treasury £m	Other £m	Total £m
Risk Weighted Assets at 1 April 2016	1,570.5	727.8	120.7	175.9	<b>2,594.9</b>
Portfolio quality increase / (decrease) in RWA	(8.8)	1.3	(29.9)	(5.7)	<b>(43.1)</b>
Portfolio size increase / (decrease) in RWA	32.6	(74.7)	4.9	5.9	<b>(31.3)</b>
<b>Risk Weighted Assets at 31 March 2017</b>	<b>1,594.3</b>	<b>654.4</b>	<b>95.7</b>	<b>176.1</b>	<b>2,520.5</b>

The Society's capital position has been enhanced through a measured balance sheet contraction programme particularly focused on higher risk non-core assets. This is reflected in the overall book quality improvement which also includes the positive benefit of decreasing loan to value ratios due to house price increases and general improving performance of the underlying residential mortgages.

The reduction in treasury related risk weighted assets is due to the relative increase in sums held with the Bank of England, which receive a zero percent weighting. These have replaced other high quality assets which are predominately weighted at 20%. The overall quality of the liquidity portfolio remains high.

## REGULATORY DEVELOPMENTS

### *Risk-based capital requirements*

For the figures above, the Society applied the Standardised Approach and has been making significant progress on its regulatory project to move to the IRB approach to calculating its capital requirements for credit risk, which commenced in October 2015.

Following a further assessment of the positive progress made to date on the IRB project the Society's Board has re-affirmed its commitment to the continued investment on the project and is indicatively targeting a submission of its application for IRB permission to the PRA in 2018.

It is the Society's current expectation that, given the nature of the Society's residential exposures, the capital required to support its credit risk should reduce under the IRB approach, resulting in a positive impact on the Society's already robust capital ratios.

## PART XVIII - SELECTED STATISTICAL INFORMATION

The following information has been extracted from the Society's management information systems. This information is unaudited. The information contained in this section should be read in conjunction with the Consolidated Historical Financial Statements and the H1 2017/8 Interim Financial Statements as well as "*Part XVI: Operating and Financial Review*".

### 1. INVESTMENT SECURITIES PORTFOLIOS

As at 31 March 2017, the Society's liquidity holdings were carried at a book value of £854 million. 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, and also for the previous two year ends.

The Society has no exposure 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.

The following table provides information on the breakdown of the Society's securities (excluding Bank of England balances or UK government debt) as at each of 31 March 2017, 31 March 2016 and 31 March 2015, respectively.

	As at 31 March		
	2017	2016	2015
	(£m)		
<b>Investment securities (available for sale)</b>			
Listed .....	385.0	359.0	274.3
Unlisted.....	-	51.1	-
<b>Total.....</b>	<b>385.0</b>	<b>410.1</b>	<b>274.3</b>

In accordance with IAS 39, available for sale investment securities are stated at fair value. 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:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
	(£m)		
<b>At beginning of year</b>	<b>410.1</b>	274.3	461.6
Additions	<b>229.9</b>	440.0	193.1
Disposals (sale and redemption)	<b>(255.5)</b>	(302.0)	(379.4)
Gains/(losses) from changes in fair value	<b>0.5</b>	(2.2)	(1.0)
<b>At end of year</b>	<b>385.0</b>	410.1	274.3

The Society considers 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 Society's activities.

### 2. LENDING AND LOAN PORTFOLIOS

As at 31 March 2017, the Society's total loans and advances to customers (including fair value adjustments for portfolio hedged risk, including accrued interest) were £4.78 billion, representing 81.9 per cent. of the Society's total assets. The Society's total assets remained stable at £5.8 billion (31 March 2016: £5.8 billion), with a 15%

increase in the prime owner occupied residential mortgage book offsetting a 14% reduction in non-core commercial balances.

Currently, no new non-conforming property lending (i.e. commercial, buy to let, sub-prime or self-certified) is being undertaken.

	<u>2017</u>	<u>2016</u> (£m)	<u>2015</u>
<b>Loans and receivables</b>			
Loans fully secured on residential property	<b>4,253.8</b>	4,131.2	3,921.4
Other loans			
Loans fully secured on land	<b>506.7</b>	584.4	713.1
Other loans	-	0.1	0.1
	<b>4,760.5</b>	4,715.7	4,634.6
<b>At fair value through profit or loss</b>			
Other loans			
Loans fully secured on land	<b>17.8</b>	26.0	44.5
	<b>4,778.3</b>	4,741.7	4,679.1
Fair value adjustment for hedged risk	<b>53.9</b>	62.0	68.0
Less: impairment provisions	<b>(55.7)</b>	(64.7)	(69.7)
	<b>4,776.5</b>	4,739.0	4,739.0

Included within loans and advances to customers for FY 2017 were £587.5 million (FY 2016: £679.6 million) of commercial lending balances.

## 2.1 Residential mortgage portfolio

### Overview

Since returning to the mortgage market in 2012/13, the Society has originated only prime residential loans. While all new lending is prime owner occupied, the Society'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 (31 March 2016: 49.8%), 42.6% buy to let (31 March 2016: 48.0%) and 1.9% other (31 March 2016: 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.

	<u>2017</u>	<u>as at 31 March</u> <u>2016</u> (£m)	<u>2015</u>
<b>Concentration by loan type</b>			
Prime owner occupied	<b>2,349.6</b>	2,045.6	1,641.2
Buy to let	<b>1,803.6</b>	1,974.7	2,156.5
Other	<b>81.9</b>	90.9	100.9
<b>Gross balances</b>	<b>4,235.1</b>	4,111.2	3,898.6
Impairment provisions	<b>(16.3)</b>	(20.8)	(23.7)
Fair value adjustments	<b>9.6</b>	13.0	13.4
	<b>4,228.4</b>	4,103.4	3,888.3



Gross residential mortgage lending in the financial year ended 31 March 2017 was £712 million (compared to £673 million in the financial year ended 31 March 2016 and £446 million in the financial year ended 31 March 2015).

### ***LTV analysis***

The table below shows analysis of the indexed loan to value distribution of the residential loan portfolio as at 31 March 2017 and 31 March 2016.

LTV Distribution	as at 31 March	
	<b>2017</b> (£m)	<b>2016</b>
>95%	<b>74.3</b>	78.8
90% - 95%	<b>73.8</b>	166.4
85% - 90%	<b>200.1</b>	326.3
75% - 85%	<b>720.0</b>	765.9
50% - 75%	<b>2,155.1</b>	1,930.8
<50%	<b>1,011.8</b>	843.0
	<b>4,235.1</b>	4,111.2

The Society's average indexed loan to value at the 31 March 2017 was 55.7% (31 March 2016: 59.9%).

### ***Arrears analysis***

Residential mortgage arrears during FY 2017 fell 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 (three months or more past due). At the year end, none remained in serious arrears.

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 31 March 2017 (31 March 2016: 1.27%).

The following tables set out the arrears for the Society's total residential mortgage portfolio (being cases three months or more in arrears expressed as a percentage of the Society's total residential mortgage loans) as at 31 March 2017, 2016 and 2015:

At 31 March 2017

	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

	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

At 31 March 2015

	Total balances	3 months+
	£m	%
Prime owner occupied	1,641.2	1.44
Buy to let	2,156.5	0.98
Other	74.5	8.88
Core residential	3,872.2	1.34
Second charge lending	26.4	10.34
Total residential including possessions	3,898.6	1.63

***Payment due status***

The table below provides further information on the Society's residential loans and advances to customers by payment due status at 31 March 2017, 31 March 2016 and 31 March 2015:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
	(£m)		
<b>Loans neither past due or impaired</b>	<b>4,156.1</b>	4,001.5	3,766.5
<b>Past due but not impaired</b>			
Past due 1 to 3 months	21.5	35.8	41.5
<b>Impaired</b>			
Not past due but impaired	20.4	21.8	-
Past due 1 to 3 months	1.9	0.8	35.1
Past due 3 to 6 months	12.5	16.2	23.3
Past due 6 to 12 months	6.5	16.0	20.0
Past due over 12 months	3.4	8.1	9.3
Possessions	12.8	11.0	2.9
	<b>4,235.1</b>	4,111.2	3,898.6

### *Collateral*

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

<b>Fair value of collateral held</b>	<b><u>2017</u></b>	<b><u>2016</u></b>	<b><u>2015</u></b>
		(£m)	
Not impaired	<b>8,132.6</b>	7,604.8	7,023.4
Impaired	<b>92.0</b>	92.5	58.0
Possessions	<b>13.7</b>	10.4	10.8
	<b>8,238.3</b>	7,707.7	7,092.2

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.

### *Forbearance strategies and renegotiated loans*

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.

A range of forbearance strategies is employed in order to work with borrowers to control arrears and, wherever possible, avoid repossession. Forbearance measures take a number of forms such as temporary reductions to contractual payments, interest capitalisation and term extensions. 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 as at 31 March 2017 and 2016:

	<b>Arrangements</b>	<b>Concessions</b>	<b>Capitalisation</b>	<b>Short-term interest only conversions</b>	<b>Term extensions</b>	<b>Total</b>
<b>31 March 2017</b>			(£m)			
<b>Loans neither past due or impaired</b>	1.7	0.2	3.3	-	2.9	<b>8.1</b>
<b>Past due but not impaired</b>						
Past due 1 to 3 months	2.9	0.4	-	-	-	<b>3.3</b>
<b>Impaired</b>						
Past due 1 to 3 months	0.5	-	-	-	-	<b>0.5</b>
Past due 3 to 6 months	5.1	0.1	-	-	0.1	<b>5.3</b>
Past due 6 to 12 months	2.8	-	-	-	0.3	<b>3.1</b>
Past due over 12 months	1.7	-	-	0.1	0.2	<b>2.0</b>
	<b>14.7</b>	<b>0.7</b>	<b>3.3</b>	<b>0.1</b>	<b>3.5</b>	<b>22.3</b>
<b>31 March 2016</b>			(£m)			
<b>Loans neither past due or impaired</b>	2.1	0.7	2.3	-	10.6	15.7
<b>Past due but not impaired</b>						
Past due 1 to 3 months	4.3	0.7	0.2	-	0.2	5.4

	Arrangements	Concessions	Capitalisation	Short-term interest only conversions	Term extensions	Total
<b>Impaired</b>						
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

The high credit quality of the residential portfolios, together with the impact of house price inflation, has led to a £3.5 million reversal of residential provision charges in FY 2017 (FY 2016: £0.2 million increase). At 31 March 2017, the Society had £16.3 million set aside for losses on residential mortgages (31 March 2016: £20.8 million).

## 2.2 Commercial mortgage portfolio

### *Commercial lending*

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 FY 2017, commercial mortgage balances excluding impairment provisions fell 14% to £588 million (FY 2016: £680 million) of which £73 million was securitised (FY 2016: £92 million) with full provision made for the residual risk to the Society.

	<b><u>FY 2017</u></b>	<b><u>FY 2016</u></b> (£m)
<b>Concentration by loan type</b>		
Loans secured on commercial property	<b>524.5</b>	610.4
Loans secured on residential property	<b>18.7</b>	20.2
<b>Gross balances</b>	<b>543.2</b>	630.6
Impairment provisions	<b>(39.4)</b>	(43.9)
Fair value adjustments	<b>44.3</b>	49.0
	<b>548.1</b>	635.7

Of the fair value adjustments for FY 2017 £40.7 million (FY 2016: £48.7 million) relate to loans secured on commercial property and £3.6 million (FY 2016: £4.2 million) relate to loans secured on residential property.

The Society's commercial real estate exposure is reasonably well spread across UK geographic regions and sectors. The commercial portfolios average indexed loan to value as at 31 March 2017 was 79.5% (31 March 2016: 82.9%).

The analysis of loans secured on commercial property (excluding the residential properties managed by West Bromwich Commercial Ltd) as at 31 March 2017 and 2016 by industry type is as follows:

	<u>at 31 March</u> <u>2017</u> (£m)	<u>2016</u>
Healthcare and leisure	139.4	167.0
Industrial and warehouse	23.3	23.1
Office	35.1	48.7
Retail	305.4	350.2
Other	21.3	21.4
	<b>524.5</b>	610.4

The table below shows the geographic spread of the commercial loan portfolio as at 31 March 2017 and 2016:

	<u>at 31 March</u> <u>2017</u> (£m)	<u>2016</u>
<b><u>Region</u></b>		
East Anglia	13.8	14.5
East Midlands	36.7	38.4
Greater London	59.1	74.1
North	34.6	41.7
North West	178.7	202.7
Scotland	12.0	16.8
South East	79.2	93.3
South West	21.4	24.4
Wales	14.3	18.7
West Midlands	49.2	59.7
Yorkshire	44.2	46.3
	<b>543.2</b>	630.6

#### *Payment due status*

The table below provides further information on the Society's commercial loans and advances to customers by payment due status at 31 March 2017, 31 March 2016 and 31 March 2015:

	<u>2017</u>	<u>2016</u>	<u>2015</u>
		(£m)	
<b>Loans neither past due or impaired</b>	<b>340.2</b>	358.4	550.9
<b>Not past due but impaired</b>	<b>69.6</b>	136.3	115.6
<b>Past due but not impaired</b>			
Past due up to 3 months	2.8	4.9	1.4
<b>Impaired</b>			
Past due up to 3 months	20.6	5.0	4.0
Past due 3 to 6 months	4.6	6.5	3.1
Past due 6 to 12 months	21.1	11.1	-
Past due over 12 months	84.3	108.4	105.5
	<b>543.2</b>	630.6	780.5

## Collateral

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

<b>Value of collateral held</b>	<b>Indexed 2017 £m</b>	<b>Unindexed 2017 £m</b>	<b>Indexed 2016 £m</b>	<b>Unindexed 2016 £m</b>
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

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 FY 2017 and FY 2016:

<b>31 March 2017</b>	<b>Arrangements</b>	<b>Capitalisation</b>	<b>Term extensions</b>	<b>Total</b>
			(£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

<b>31 March 2016</b>	<b>Arrangements</b>	<b>Capitalisation</b>	<b>Term extensions</b>	<b>Total</b>
			(£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

Impairment provisions are held in relation to both the performing and non-performing segments of the commercial lending portfolio. The de-risking of the balance sheet has continued with a 14% decrease in exposure to non-core commercial balances from £680 million in FY 2016 to £588 million in FY 2017. Some £73 million of this exposure was in securitisation vehicles which have the effect of transferring the risk of loss out of the Society. Of the remaining £515 million of exposure, £302 million are non-performing loans being managed for recovery and £38 million (7%) has been set aside as provisions in respect of these non-securitised commercial loans.

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 £7.0 million 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 £3.5 million. A 0.25% increase in expected exit yield requirements would increase provisions by £8.6 million.

The Society recognised commercial impairment charges of £11.1 million in FY 2017 compared with £7.9 million 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. Provisions held for commercial impairment were £39.4 million at 31 March 2017 (31 March 2016: £43.9 million), equivalent to 6.7% of the current loan book (31 March 2016: 6.5%).

A key strategy in mitigating the losses incurred on commercial loans is identifying circumstances whereby the appointment of an 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 (31 March 2016: 46%).

## PART XIX - RISK MANAGEMENT

### OVERVIEW

Effective management of risks and opportunities is essential to achieving the Society's strategic objectives. The Society aims to manage effectively all of 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 appropriate controls to manage these exposures within the Board's agreed risk appetite.

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 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.

### 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, capital, credit, liquidity, market, basis, operational, retail conduct, information and pension liability (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
<b>First</b>	Business Operations	Line Management	Line Management Oversight
<b>Second</b>	Policy, Controls, Measure, Monitor	Control Functions	Management and Board Committees
<b>Third</b>	Assurance	Internal Audit	Audit Committee

### GOVERNANCE STRUCTURE

Risk governance is 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.

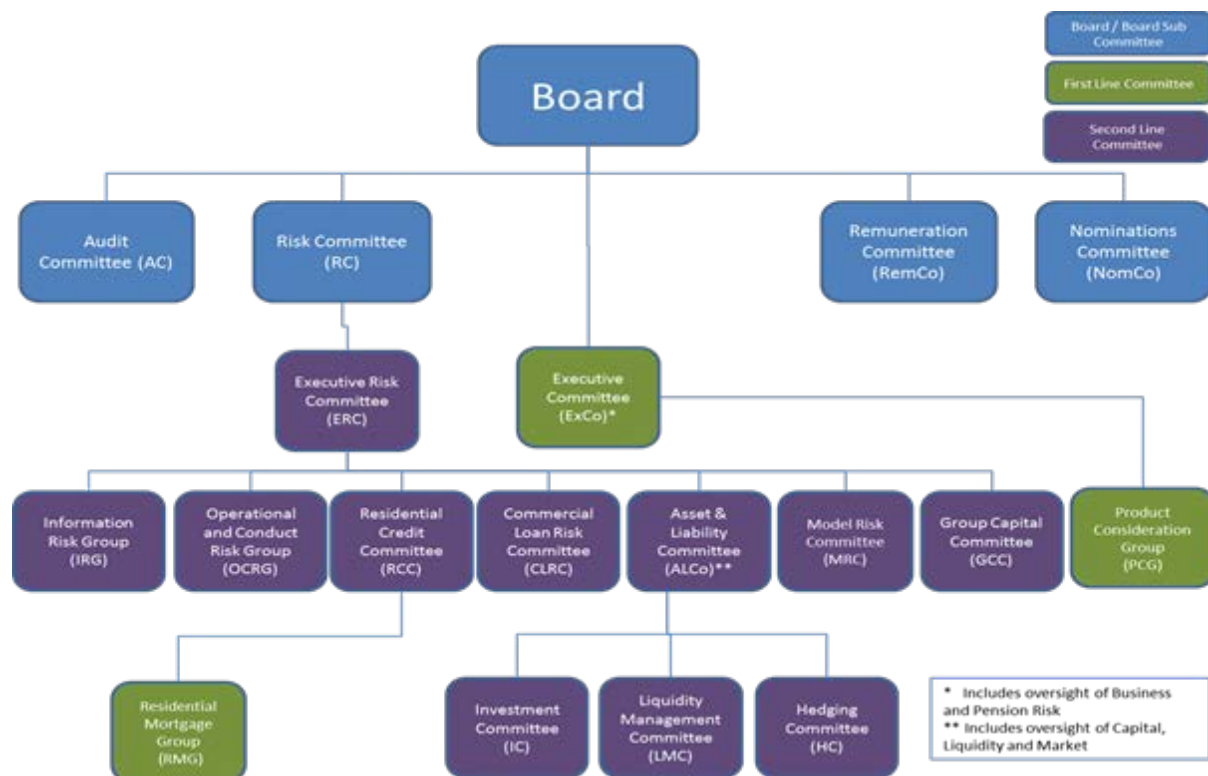
**Group Capital Committee (GCC)** - This Committee is chaired by the Group Finance & Operations Director and is responsible for reviewing the Group's capital requirements.

**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.

**Model Risk Committee (MRC)** – This committee is chaired by the Group Finance & Operations Director and is responsible for approving and routinely reviewing performance of the Society's high materiality models.

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

The Risk Committee hierarchy is represented in the following diagram:



## 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 that assets and liabilities reprice at different times and / or by varying amounts, adversely affecting the net interest margin;

**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; and

**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.

**BUSINESS CONDITIONS AND THE ECONOMIC ENVIRONMENT**

The Society is exclusively focused in the UK and, therefore, the general UK macro-economic environment is key to its success. Early Brexit discussions have done little to alleviate market uncertainty. Following an indecisive result to the snap general election, there is a real possibility that the UK government, although currently optimistic, will be unable to negotiate a trade deal with the EU, an eventuality with, as yet, unknown consequences.

Despite the doubt enshrouding the overall economy, the residential mortgage markets appear reasonably buoyant. Whilst the TFS, launched during FY 2017, has supported the market by providing low cost four year funding, it has contributed to highly competitive mortgage pricing. Following closure of the TFS to new commitments on 28 February 2018, the markets need to adjust to the removal of this BoE stimulus. The Society will continue to monitor developments in this area and consider the impact on its lending and funding plans.

The non-core commercial loan book has historically proven sensitive to a downturn in the economic environment. While the Group's exposure to this sector is steadily reducing, there remains the risk of further commercial impairment provision requirements.

Residential borrowers have experienced a squeeze on earnings, with inflation outstripping wage increases, and the first interest rate rise in over 10 years to 0.5% in November 2017. The markets anticipate that rates will rise further, albeit following a gradual upward trend. The Society's residential mortgage portfolios are of a high

credit quality and therefore able to withstand some deterioration in economic conditions before losses are incurred.

The new accounting standard IFRS 9 'Financial Instruments', applied by the Group from 1 April 2018, encapsulates a range of economic scenarios in its determination of impairment provision requirements which must be recognised on an expected, rather than incurred, loss basis. An intended consequence of IFRS 9 is that banks and building societies will recognise credit losses earlier than under current accounting standards. The Society's IFRS 9 project is progressing to timetable.

The Society recognises the ongoing need to invest in its technological capabilities. Technology is fundamental to delivering growth, excellent customer service and a robust defence against cyber risks. Against the recent backdrop of low interest rates, political upheaval and economic uncertainty the Society has demonstrated the ability to grow its prime residential mortgage book, exit non-core activities in a controlled manner, deliver healthy and sustainable underlying profits, invest in the future and comfortably meet all regulatory capital and liquidity requirements. The Society will move forward with each of these critical objectives for the remainder of the financial year maintaining emphasis, as always, on helping more borrowers to purchase their own homes and enabling savers to prepare and plan for a secure future.

**The external factors that impact the Society include:**

- Interest rates (Bank of England 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.

**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.

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.

### Residential Mortgage 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 (31 March 2016: 49.8%), 42.6% buy to let (31 March 2016: 48.0%) and 1.9% other (31 March 2016: 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.

High quality lending, effective credit risk management practices focused on assessing credit worthiness and falling unemployment have all contributed to sustained low levels of arrears. At 31 March 2017, just 0.81% (31 March 2016: 1.27%) of accounts were three months or more in arrears. This compares favourably with data from the CML 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% as at 31 March 2017 (31 March 2016: 1.07%).

As illustrated in the analysis table below, the regional spread of residential property assets in the UK 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.

#### As at 31 March 2017

REGION	2017 £m	2016 £m
East Anglia	122.7	110.7
East Midlands	415.3	380.7
Greater London	553.6	591.2
Northern Ireland	5.2	5.8
North	164.2	147.7
North West	496.1	460.8
Scotland	116.2	126.8
South East	751.7	742.1
South West	353.4	336.5

Wales	<b>207.6</b>	194.7
West Midlands	<b>705.7</b>	713.1
Yorkshire	<b>343.4</b>	301.1
	<b>4,235.1</b>	4,111.2

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 agreed strategy will reflect the customer’s individual circumstances and will be used in line with industry guidance.

For further discussion of the Society’s residential mortgage lending, see section 2 (*Lending and Loan Portfolios*) in “*Part XVIII: Selected Statistical Information*”.

### **Commercial Mortgage Lending**

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

The Society’s 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 £588 million at 31 March 2017 (31 March 2016: £680 million) of which £73 million was securitised (31 March 2016: £92 million) with full provision made for the residual risk to the Society.

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.

For further discussion of the Society’s commercial mortgage lending, see section 2 (*Lending and Loan Portfolios*) in “*Part XVIII: Selected Statistical Information*”.

### **Analysis of treasury credit risk exposures**

For further information, see “*Part XVI – Operating and Financial Review – 8.6 Treasury assets*”.

## **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 Risk 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 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 BoE 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 BoE 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 BoE 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, repricing 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 PRA. The levels of Group pre-tax interest rate risk exposures to a 2% parallel shift, through the reporting period were as follows:

	<u>At 31 March 2017</u>	<u>Average</u>	<u>High</u>	<u>Low</u>
		(£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 £13.4 million (FY 2016: £47.9 million) 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

## 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 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 Group's liquidity risk is managed as follows:

- The Board has delegated authority for the management of liquidity risk to the 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 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 PRA'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 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. The Society is responsible for the liquidity and cash flow requirements of wholly owned subsidiaries.

The tables below analyse the Group's assets and liabilities across maturity periods that reflect the residual maturity from the year end date to the contractual maturity date as at 31 March 2017 and 2016. The actual repayment profile of loans and advances is likely to be significantly different to that shown in the analysis.

<b>At 31 March 2017</b>	<b>Repayable on demand</b>	<b>Less than 3 months</b>	<b>3 to 12 months</b>	<b>1 to 5 years (£m)</b>	<b>Over 5 years</b>	<b>No specific maturity</b>	<b>Total</b>
<b>Assets</b>							
Cash and balances with the Bank of England	287.6	-	-	-	-	7.2	<b>294.8</b>
Loans and advances to credit institutions	52.1	121.9	-	-	-	-	<b>174.0</b>
Investment securities	-	13.7	152.1	219.2	-	-	<b>385.0</b>
Derivative financial instruments	-	2.2	0.1	2.5	1.5	-	<b>6.3</b>
Loans and advances to customers	-	284.9	73.9	319.2	4,098.5	-	<b>4,776.5</b>
Deferred tax assets	-	-	-	-	-	16.4	<b>16.4</b>
Trade and other receivables	-	-	-	-	-	3.5	<b>3.5</b>

Intangible assets	-	-	-	-	-	13.3	<b>13.3</b>
Investment properties	-	-	-	-	-	128.9	<b>128.9</b>
Property, plant and equipment	-	-	-	-	-	32.1	<b>32.1</b>
	<b>339.7</b>	<b>422.7</b>	<b>226.1</b>	<b>540.9</b>	<b>4,100.0</b>	<b>201.4</b>	<b>5,830.8</b>
<b>Liabilities and equity</b>							
Shares	3,150.6	123.6	179.5	973.6	-	-	<b>4,427.3</b>
Amounts due to credit institutions	-	135.7	90.5	224.1	-	-	<b>450.3</b>
Amounts due to other customers	7.3	74.9	49.5	1.0	-	-	<b>132.7</b>
Derivative financial instruments	-	0.1	3.4	16.8	48.7	-	<b>69.0</b>
Debt securities in issue	-	58.0	-	145.7	59.5	-	<b>263.2</b>
Deferred tax liabilities	-	-	-	-	-	5.0	<b>5.0</b>
Trade and other payables	-	-	-	-	-	10.2	<b>10.2</b>
Provisions for liabilities	-	-	-	-	-	3.1	<b>3.1</b>
Retirement benefit obligations	-	-	-	-	-	6.5	<b>6.5</b>
Profit participating deferred shares	-	-	-	-	-	173.0	<b>173.0</b>
Subscribed capital	-	-	-	-	-	75.0	<b>75.0</b>
General reserves	-	-	-	-	-	211.0	<b>211.0</b>
Revaluation reserve	-	-	-	-	-	3.5	<b>3.5</b>
Available for sale reserve	-	-	-	-	-	1.7	<b>1.7</b>
Cash flow hedging reserve	-	-	-	-	-	(0.7)	<b>(0.7)</b>
	<b>3,157.9</b>	<b>392.3</b>	<b>322.9</b>	<b>1,361.2</b>	<b>108.2</b>	<b>488.3</b>	<b>5,830.8</b>

At 31 March 2016	Repayable on demand	Less than 3 months	3 to 12 months	1 to 5 years (£m)	Over 5 years	No specific maturity	Total
<b>Assets</b>							
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
	<b>289.1</b>	<b>514.8</b>	<b>193.2</b>	<b>574.8</b>	<b>3,998.8</b>	<b>196.4</b>	<b>5,767.1</b>
<b>Liabilities and equity</b>							
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)
	<b>3,363.8</b>	<b>320.8</b>	<b>410.5</b>	<b>1,028.8</b>	<b>122.9</b>	<b>520.3</b>	<b>5,767.1</b>

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.

Liquidity management is key to ensuring the Society can fulfil its regulatory and operational obligations whilst controlling the cost of holding liquid assets. 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 BoE 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 £57 million of gilts, obtained under an asset swap agreement, which are not included in Group liquidity but do qualify as buffer liquidity for regulatory purposes (31 March 2016: £137 million treasury bills obtained under the FLS).

There was no impairment provision requirement for treasury assets at 31 March 2017 (31 March 2016: nil, 31 March 2015: nil). An analysis of the liquidity portfolio is set out in the table 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
<b>Total buffer liquidity</b>	<b>626.7</b>	<b>73.4</b>
Other securities - rated single A or better	45.8	5.4
Subsidiary/other liquidity	181.3	21.2
<b>Total liquidity</b>	<b>853.8</b>	<b>100.0</b>

#### 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
<b>Total buffer liquidity</b>	<b>495.6</b>	<b>59.7</b>
Other securities - rated single A or better	123.2	14.9
Subsidiary/other liquidity	210.7	25.4
<b>Total liquidity</b>	<b>829.5</b>	<b>100.0</b>

The following table is an analysis of the gross contractual cash flows payable under financial liabilities:

At 31 March 2017	Less than 3 months	3 to 12 months	1 to 5 years (£m)	Over 5 years	Total
<b>Liabilities</b>					
Shares	4,011.1	185.8	266.5	-	<b>4,463.4</b>
Amounts due to credit institutions and other customers	202.0	141.2	227.3	74.9	<b>645.4</b>
Debt securities in issue	58.3	2.0	153.0	104.6	<b>317.9</b>
Derivative financial instruments	3.7	13.6	45.3	25.0	<b>87.6</b>
	<b>4,275.1</b>	<b>342.6</b>	<b>692.1</b>	<b>204.5</b>	<b>5,514.3</b>

At 31 March 2016	Less than 3 months	3 to 12 months	1 to 5 years (£m)	Over 5 years	Total
<b>Liabilities</b>					
Shares	<b>3,815.8</b>	<b>345.8</b>	<b>251.2</b>	-	<b>4,412.8</b>
Amounts due to credit institutions and other customers	<b>146.8</b>	<b>179.4</b>	<b>72.0</b>	<b>74.9</b>	<b>473.1</b>
Debt securities in issue	<b>1.5</b>	<b>4.0</b>	<b>302.9</b>	<b>118.2</b>	<b>426.6</b>
Derivative financial instruments	<b>7.4</b>	<b>21.0</b>	<b>77.5</b>	<b>86.0</b>	<b>191.9</b>
	<b>3,971.5</b>	<b>550.2</b>	<b>703.6</b>	<b>279.1</b>	<b>5,504.4</b>

## **CAPITAL RISK**

The Society conducts an 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.

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.

## **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 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, provides 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	<p>Adverse changes to the operating environment arising from the general uncertainty in the UK economy, following the Brexit Vote and the 2017 general election, leading to:</p> <ul style="list-style-type: none"> <li>• 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;</li> <li>• Reduced activity in the housing market and possible adverse impact from both lower lending and a potential fall in house prices;</li> <li>• Increased competition and cost of retail funding;</li> <li>• Low or flat economic growth; and</li> <li>• Increasing regulatory costs.</li> </ul>	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 BoE 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 resources.
	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.
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.
Liquidity risk	Intensification of competition for retail funding.	The Society continues to attract new retail savers despite intense competition.

<b>Risk category</b>	<b>Principal external threats</b>	<b>Society response and mitigants</b>
Market risk/ Basis risk	Reduction in returns from residential tracker mortgage assets whose rate is linked to BoE 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.

## **PART XX - SUPERVISION AND REGULATION**

### **1. EUROPEAN UNION LEGISLATION**

The framework for supervision and regulation of banking and financial services in the UK has been, and continues to be, heavily influenced by European Union legislation. The principal intention underlying CRD IV is the harmonisation of banking regulation and supervision throughout the EEA. CRD IV prescribes minimum standards in key areas and requires EEA member states to give “mutual recognition” to each other’s authorisation and prudential supervision systems. CRD IV also contains a “passport” concept, which amounts to freedom for a credit institution authorised in its “home” state to establish branches in, and to provide cross-border services into, other EEA member states.

Although credit institutions are primarily regulated in their home state by a local regulator, the CRD IV prescribes minimum criteria for regulation of the authorisation of credit institutions and the prudential supervision applicable to them. The Society’s local regulators are the PRA and the FCA. For further information about regulation in the UK see paragraph 2 “*UK Regulation*” below. CRD IV substantially reflects the Basel III capital and liquidity standards. CRD IV also makes provision for (among other things) requirements to reduce reliance by credit institutions on external credit ratings, by requiring that all banks’ investment decisions are based not only on ratings but also on their own internal credit opinion, and that banks with a material number of exposures in a given portfolio develop internal ratings for that portfolio instead of relying on external ratings for the calculation of their capital requirements. Certain details remain to be clarified in further technical standards to be produced by the EBA.

The CRR gives express recognition for CET1 capital instruments for mutual’s and co-operatives and permits the use of a cap or restriction to safeguard the interests of members and reserves.

### **2. UK REGULATION**

The UK Financial Services Act 2012 amended certain existing legislation including the Financial Services and Markets Act 2000, the Act and the Banking Act to make provision about the exercise of certain statutory functions relating to building societies.

Another area of change which impacts on the UK regulatory landscape relates to banking reform. The Banking Reform Act introduced amendments to FSMA which provide for, inter alia, the ring-fencing of vital banking services from international and investment banking services, measures on loss absorbency and depositor preference and measures intended to enhance competition in the banking sector. Certain aspects of such measures entered into force on 1 January 2015 although the full ring-fencing regime will not apply until 2019. Further, the Government has carved building societies out of the proposed ring-fencing legislation and, instead, reserves the power to amend the Act to bring building societies legislation into line with the proposed ring-fencing requirements.

The PRA has also published Policy Statement 21/16 on “Ensuring operational continuity in resolution” on 7 July 2016, containing rules which will apply from 1 January 2019. The rules support the resolvability and resilience of building societies and banks in seeking to ensure critical shared services are organized to facilitate continuity in the event of failure.

On 1 January 2015, the Banks and Building Societies (Depositor Preference and Priorities) Order 2014 came into force, changing the different creditor ranking that previously would have applied in the event of a liquidation between a bank and a building society. The effect of these changes is that both banks and building societies are now subject to the preference in ranking accorded to retail deposits and a super-preference for deposits covered by the FSCS. When combined with other specific changes affecting building societies, the relative differences in ranking as between banks and building societies no longer apply and the effective creditor hierarchy for banks and building societies is now the same.



## 2.1 The UK Building Societies Act

The main legislation regulating building societies is the Act. The Act governs the creation, authorisation and management of building societies. The Society is regulated by the FCA in relation to conduct of business matters and by the PRA in relation to prudential requirements. With the introduction of the FSMA, certain sections of the Act were repealed. However, a substantial part of the Act, including the constitutional parts dealing with the principal purpose of building societies, nature limits and general governance, among others, still remain in force. The Act has been amended and supplemented since its introduction by secondary legislation. For further information on the reforms under the Financial Services and Markets Act 2000, see below.

On 6 July 2012, HM Treasury published a discussion document entitled: “The future of building societies” which set out the Government’s aim to maintain the distinctiveness of the building society sector while creating a level playing field and removing unnecessary barriers to growth. The Government stated its intention to amend the Act to widen the opportunities for building societies without compromising their mutuality. As a result, modernising changes to the Act were made under the Banking Reform Act to bring it more in line with company law, assist building societies in raising funding and make minor technical changes in order to allow the building society sector to compete on a more level playing field with banks. The changes, in particular:

- facilitate electronic communications with members;
- remove the restrictions on building societies relating to floating charges;
- make it easier for building societies to accept small business deposits by making adjustments to the funding limit calculation;
- make certain changes concerning the distribution of shares on the transfer of a building society’s business on a demutualisation; and
- permit holders of deferred shares of less than two years’ standing to be eligible to receive shares or cash when a society demutualises (thereby removing the risk that tier 1 capital would be downgraded to tier 2 capital in the event of such a demutualisation). It should be noted that the risk alluded to in relation to any such downgrade is addressed in relation to CCDS by ensuring that CCDS will be represented by a global certificate which will be registered in the name of the Nominee for the Clearing Systems.

All of these changes to the Act are in force.

## 2.2 Building societies regulation

The following sections describe some of the concepts for a building society which is authorised under the FSMA.

### *Mutuality*

Building societies are mutual organisations that are managed for the benefit of their members, who are primarily retail savings and residential mortgage customers. Each member is normally entitled to one vote at a building society’s general meeting, regardless of the size of the member’s deposit account or mortgage loan or the number of accounts the member maintains.

### *Purpose*

Building societies are required to be engaged primarily in the business of making loans secured on residential property, which are substantially funded by members. In addition, as long as building

societies comply with specific limits on lending and funding, they may engage in additional activities such as commercial lending, unsecured personal lending, insurance and personal investment product activities, subject to compliance with regulatory requirements of the FCA, the PRA and the CMA. The general restriction which used to apply to building societies from creating floating charges was removed by the Banking Reform Act with effect from 26 March 2015.

Building societies have a statutory duty to keep accounting records as well as establish and maintain systems of control. The FCA and the PRA are empowered to request *ad hoc* reports regarding a society's compliance with these requirements.

### ***Nature of membership***

The members of a building society fall into two categories. The first category consists of investing or "shareholding" members. Shareholding members are individuals who have made a deposit (also referred to as an investment) in a share account with a building society or who hold deferred shares in the society, and bodies corporate which hold deferred shares. In this Part XX, deposits in these share accounts are referred to as "UK retail member deposits" and people holding UK retail member deposits are referred to as "UK retail member depositors". Deferred shares include the Society's PPDS, PIBS and, once issued, CCDS.

There are restrictions on building societies raising funds from individuals other than in the form of deposits in share accounts or by the issue of deferred shares (including PIBS and, once issued, the CCDS (see further below)). A subsidiary of a building society may, however, offer deposit accounts which do not confer member status provided it has the required regulatory authorisation. Deposits in these accounts are referred to as "non-member deposits".

The second category of members are "borrowing" members, that is, individuals who have received a loan from the building society (or in certain cases, if the rules of the society allow, from another person who holds the benefit of the loan for the building society) which is fully or, if the rules of the society allow, substantially secured on land. Building societies may also make loans that do not confer member status, which generally consist of unsecured loans.

### ***Limitations on funding and lending***

The Act imposes limits on the ability of building societies to raise funds and to make loans. Investing shares in a building society, representing UK retail member deposits made with the society, must account for not less than 50 per cent. of its total funding.

Loans made by a building society and its subsidiaries which are fully secured on residential property must account for not less than 75 per cent. of its total trading assets (that is, the total assets of a building society and its subsidiaries, plus provisions for bad or doubtful debts, less liquid assets, fixed assets and certain long-term insurance funds).

### ***Building Societies (Financial Assistance) Order 2010***

On 7 April 2010, the Building Societies (Financial Assistance) Order 2010 (the **Financial Assistance Order**) came into force in exercise of certain powers under the Banking Act for the purpose of modifying the application of the Act in specified circumstances to facilitate the provision of relevant financial assistance (including the giving of guarantees or indemnities or any other kind of financial assistance (actual or contingent)) by certain 'qualifying institutions'. Qualifying institutions for this purpose include HM Treasury, the BoE, another central bank of a Member State of the EEA, the European Central Bank, or any person acting for or on behalf of any of such institution or providing financial assistance to a building society on the basis of financial assistance received from such an institution. Most significantly, the Financial Assistance Order permits any qualifying institution to provide such assistance without it counting for the purpose of the 50 per cent. limit on the building

society's non-member funding and the Financial Assistance Order also modifies the application of the purpose test and the lending limit.

### *Nature of capital*

UK retail member deposits are classified as shares in a building society's balance sheet. There is a fundamental distinction between a share in a building society and a share in a limited liability company. Holders of ordinary shares in a company normally do not have the right to withdraw their share capital from the company. The share capital of a company is therefore fixed. A UK retail member depositor has a right to withdraw his or her investment from a building society. The share capital of a building society therefore fluctuates each time UK retail member depositors deposit or withdraw funds from their account. As a result shares in a building society do not form a permanent capital resource.

The permanent capital of a building society consists primarily of its reserves (which have been built up over the years mainly from its retained earnings), any deferred shares that it has issued and tier 2 subordinated debt. Prior to the development of CCDS, the deferred shares issued by the Society were mainly in the form of PIBS and PPDS, which historically counted towards a society's 'core tier 1 capital' (the predecessor to common equity tier 1 capital). Changes to the capital adequacy framework which were implemented in the UK at the end of 2010, toughened the requirements for tier 1 capital. PIBS, which were already in existence, retained their capital status but the extent to which such deferred shares count towards regulatory capital is being phased out over a long transitional period. CCDS meet the regulatory criteria for Common Equity Tier 1 capital, while being consistent with the values of mutuality and supporting members' interests. The CCDS are also designed to be a suitable instrument for raising new capital from external investors.

### *Hedging*

The Act prohibits building societies and their subsidiaries from entering into any transaction involving derivative instruments unless the transaction falls within one of the specified exceptions, including where it is entered for the purpose of limiting the extent to which the society will be affected by fluctuations in interest rates, exchange rates, any index of retail prices, any index of residential property prices, any index of the prices of securities or the ability or willingness of a borrower to repay a loan owing to the building society.

### *Demutualisation*

The Act permits a building society to demutualise by transferring the whole of its business to an existing company (referred to as a **takeover**) or to a specially formed company (referred to as a **conversion**) so long as the process meets statutory requirements. Any such demutualisation must be approved by members and confirmed by the PRA. The successor company will be a bank, which must be duly authorised to carry on its deposit-taking business by the PRA or equivalent EEA regulatory authority.

The member approval threshold required varies depending on the type of demutualisation. In order to convert into a new bank by transferring the building society's business to a specially formed company, a minimum of 50 per cent. of shareholding members qualified to vote would have to vote on a requisite shareholders' resolution, and a minimum of 75 per cent. of those voting would have to support the resolution to convert. In addition, more than 50 per cent. of borrowing members who vote would have to vote in favour of a borrowing members' resolution to convert. On a demutualisation as a result of a takeover by an existing bank or other company, the requirements would be similar except that 50 per cent. of shareholding members qualified to vote (or shareholding members representing 90 per cent. by value of the society's shares) must actually vote in favour of the requisite shareholding members' resolution.

### *Mutual society transfers*

The Act (as modified by the Mutual Societies (Transfers) Order 2009) permits a building society to transfer the whole of its business to the subsidiary of another mutual society (as defined in section 3 of the Building Societies (Funding) and Mutual Societies (Transfers) Act 2007 (the **Funding and Mutual Societies Transfers Act**). The successor subsidiary must be duly authorised to carry on its deposit-taking business by the PRA or an equivalent EEA regulatory authority. The terms of the transfer to the relevant subsidiary must include provision for making membership of the holding mutual (or membership of the parent undertaking of such holding mutual) available to every qualifying member of the building society and to every person who, after the transfer, becomes a customer of the company, and the membership of the holding mutual (or such parent undertaking) must be on terms no less favourable than those enjoyed by existing members of the holding mutual (or such parent undertaking, as the case may be).

A transfer of business to a subsidiary of another mutual society requires approval by members and confirmation by the PRA. The member approval thresholds require a shareholding members' resolution to be passed by a minimum of 75 per cent. of shareholding members qualified to vote and voting on the resolution and a borrowing members' resolution to be passed by more than 50 per cent. of borrowing members qualified to vote and voting on the resolution.

### *Directed transfers*

The Act confers power on the PRA, if it considers it expedient to do so in order to protect the investments of shareholders or depositors, to direct a building society to transfer all of its engagements to one or more other building societies or to transfer its business to an existing company. The Financial Services Act 2012 (the **FS Act**) also amended the Act to extend this power of direction to a transfer of a building society's business to an existing or specially formed company that is a subsidiary of another mutual society (as defined in section 3 of the Funding and Mutual Societies Transfers Act). Where any such direction is made, the PRA may also, if it considers it expedient to do so in order to protect the investments of shareholders or depositors, direct that such transfer may proceed on the basis of a resolution of the board of directors of the building society, without the need for member approval.

## **2.3 The UK regulators**

The PRA is currently the prudential regulator for building societies, banks, insurance companies and other deposit takers. The general objective of the PRA is promoting the safety and soundness of PRA-authorised persons.

The PRA supervises and regulates financial institutions, including building societies, on an ongoing basis by continually assessing their risk profile and capacity to manage and control risks. If the PRA finds that a financial institution has failed to comply with the requirements under the Financial Services and Markets Act 2000, the PRA has a variety of enforcement powers including:

- issuing a private warning; or
- taking disciplinary measures, such as issuing a public statement of misconduct or imposing a financial penalty.
- The FCA is currently the conduct regulator for firms that are prudentially regulated by the PRA (dual-regulated firms). The FCA regulates both prudential and conduct matters for all other firms. The FCA's strategic objective is ensuring the relevant markets function well. The FCA's operational objectives are:
- the consumer protection objective;

- the integrity objective; and
- the competition objective.

The FCA also has a variety of enforcement powers under the Financial Services and Markets Act 2000, and from 1 April 2014, is responsible for supervision of consumer credit regulation and superintendence and enforcement of the CCA, as amended.

As set out below, the CMA also enjoys certain enforcement powers under the UK financial services regime.

## 2.4 Authorisation under the FSMA

The FSMA prohibits any person from carrying on a “regulated activity” by way of business in the UK unless that person is authorised or exempt under the FSMA. Regulated activities include: deposit-taking, mortgage activities (such as entering into, administering, or advising or arranging in respect of, regulated mortgage contracts), consumer credit activities (such as credit broking, lending, administration and collection), effecting and carrying out contracts of insurance as well as insurance mediation, and investment activities (such as dealing in investments as principal or as agent, arranging deals in investments, and managing investments). The Society is authorised for, among other things, deposit-taking, mortgage and certain investment activities. It is also authorised for various consumer credit activities. The FSMA also prohibits financial promotions in the UK unless the promotion is issued or approved by an authorised person or is exempt from such requirements.

The FSMA (as amended by the FS Act) imposes an ongoing system of regulation and control on building societies. The detailed rules and prudential standards set by the FCA and the PRA are contained in various parts of the FCA Handbook and the PRA Rulebook together with guidance in various policy statements and supervisory statements.

## 2.5 Lending

### *Consumer credit*

The regulatory framework in this area consists of the FSMA and secondary legislation and the CCA and secondary legislation, together with the FCA Handbook including the Consumer Credit sourcebook. A “regulated credit agreement” is defined as follows:

- For agreements entered into on or after 1 April 2014 article 60B of the Financial Services and Markets Act 2000 (Regulated Activities) Order 2001 (**RAO**) provides that a regulated credit agreement is an agreement among: (i) an individual, (ii) a partnership consisting of two or three persons not all of whom are bodies corporate, or (iii) an unincorporated body of persons which does not consist entirely of bodies corporate and is not a partnership between (“A”) and any other person (“B”) under which B provides A with credit of any amount, and which is not an exempt agreement within the RAO.
- For agreements entered into before 1 April 2014, a credit agreement which was a regulated credit agreement pursuant to section 8 of the CCA at the time the agreement was entered into (or became such an agreement after being varied or supplemented by another agreement before April 1, 2014), excluding those agreements which would now be regulated mortgage contracts or regulated home purchase plans under the RAO.

If requirements under the CCA as to entering into, documenting and servicing a regulated credit agreement are not or have not been met, then the agreement is unenforceable against the borrower without a court order or (for agreements entered into before 6 April 2007) is totally unenforceable, depending on the circumstances. Under sections 75 and 75A of the CCA, in certain circumstances a

lender is liable to a customer in relation to misrepresentation and breach of contract by a supplier in a transaction financed by a credit agreement regulated by the CCA or treated as such, and the lender has a statutory indemnity from the supplier against liability under section 75, subject to any agreement between the lender and the supplier.

If prohibitions under FSMA as to authorisation or financial promotions are contravened (by credit brokers as well as lenders like us), then the affected regulated credit agreement is unenforceable against the borrower without a validation order from the FCA.

### *Mortgage lending*

FSMA, together with the RAO regulates mortgage credit within the definition of “regulated mortgage contract” and also regulates certain other types of home finance. A credit agreement is a regulated mortgage contract if it is entered into on or after 31 October 2004 and, at the time it is entered into: (a) the credit agreement is one under which the lender provides credit to an individual or to trustees; (b) the contract provides for the repayment obligation of the borrower to be secured by a first legal mortgage on land (other than timeshare accommodation) in the UK; and (c) at least 40 per cent. of that land is used, or is intended to be used, as or in connection with a dwelling by the borrower or (in the case of credit provided to trustees) by an individual who is a beneficiary of the trust, or by a related person. From 21 March 2016, the definition of regulated mortgage contract has changed in line with the UK’s implementation of the Mortgage Directive. Importantly, a mortgage no longer needs to be a first charge mortgage to fall within the definition of a regulated mortgage contract. This and other changes to mortgage regulation as a result of the implementation of the Mortgage Directive are described in the “*Mortgage Directive*” section below.

If prohibitions under the FSMA as to authorisation or financial promotions are contravened (by mortgage intermediaries as well as lenders), then the affected regulated mortgage contract (and, in the case of financial promotions, other credit secured on land) is unenforceable against the borrower without a court order. The FCA’s Mortgages and Home Finance: Conduct of Business sourcebook (**MCOB**) sets out rules in respect of regulated mortgage contracts and certain other types of home finance. Under MCOB rules, an authorised firm (such as the Society) is restricted from repossessing a property unless all other reasonable attempts to resolve the position have failed, which can include the extension of the term of the mortgage, product type changes and deferral of interest payments.

Any credit agreement intended to be a regulated mortgage contract or unregulated may instead be wholly or partly regulated by the CCA or treated as such. Any credit agreement intended to be regulated by the CCA or treated as such or unregulated may instead be a regulated mortgage contract. This is because of technical rules on determining whether the credit agreement or any part of it falls within the definition of a regulated mortgage contract under the RAO or within the definition of a regulated agreement under the CCA (described below) and technical rules on changes to credit agreements.

## **2.6 Mortgage Directive**

On 31 March 2011, the European Commission published a proposal for a directive on credit agreements relating to residential immovable property for consumers. The Council of the European Union adopted the Mortgage Directive (Directive 2014/17/EU) on 28 January 2014 and it was published in the Official Journal of the European Union on 28 February 2014. It entered into force twenty days after such publication and was implemented by the UK with effect from 21 March 2016.

The Mortgage Directive applies to: (a) credit agreements secured by a mortgage or comparable security commonly used in a member state of the EU (a Member State) on residential immovable property, or secured by a right relating to residential immovable property and (b) credit agreements the purpose of which is to provide finance to purchase or retain rights in land or in an existing or proposed residential building, and also extends the Consumer Credit Directive (2008/48/EC) to unsecured credit agreements

the purpose of which is to renovate residential immovable property involving a maximum total amount of credit of EUR 75,000. The Mortgage Directive does not apply to certain equity release credit agreements to be repaid from the sale proceeds of an immovable property, or to certain credit granted by an employer to its employees but does apply to buy to let mortgages.

The Mortgage Directive requires (among other things): standard information in advertising; standard pre-contractual information; adequate explanations to the borrower on the proposed credit agreement and any ancillary service; calculation of the annual percentage rate of charge in accordance with a prescribed formula; assessment of creditworthiness of the borrower and a right of the borrower to make early repayment of the credit agreement. The Mortgage Directive also imposes prudential and supervisory requirements for credit intermediaries and non-bank lenders.

For the most part, the UK Government has sought to put in place what it has described as the minimum requirements to meet its legal obligations under the Mortgage Directive in respect of buy-to-let mortgages. The legislation provides that firms do not need to apply the UK Government's appropriate framework for buy-to-let mortgages where a borrower is acting wholly or predominantly for the purposes of a business. HM Treasury has stated that they would expect consumer buy-to-let activity to represent a small proportion of total buy-to-let transactions. Generally speaking, the Mortgage Directive does not apply to credit agreements existing before 21 March 2016. However, the UK's implementation of the Mortgage Directive also operates to retrospectively regulate certain credit agreements secured on land that were in existence at 21 March 2016, including existing second charge mortgages (consumer credit back book mortgage contracts). Certain provisions of MCOB will become applicable to these consumer credit back book mortgage contracts. These include the rules relating to post-sale disclosure (MCOB 7), charges (MCOB 12) and arrears, payment shortfalls and repossessions (MCOB 13). General conduct of business standards will also apply (MCOB 2). This process is subject to detailed transitional provisions that are intended to retain certain customer protections in CONC and the CCA that are not contained within MCOB.

Any further changes in the legislative or regulatory framework for mortgage regulation, including as a result of implementation of the Mortgage Directive into UK law, or any future review carried out by the FCA, or any changes to the FCA Handbook Rules, may adversely affect the Society's businesses and operations.

## **2.7 Insurance**

The Society is also authorised for carrying out insurance mediation. The Insurance: Conduct of Business sourcebook, which is part of the FCA Handbook, sets out rules in respect of non-investment insurance.

## **2.8 Financial Services Compensation Scheme**

The FSMA established the Financial Services Compensation Scheme, or FSCS, which pays compensation to eligible customers of authorised financial services firms which are unable, or are likely to be unable, to pay claims against them. The levels of compensation are, for example, for claims against firms declared in default on or after 1 January 2010 (30 January 2017 for deposits): (i) for retail deposits, 100 per cent. of the first £85,000; (ii) for mortgage advice and arranging, 100 per cent. of the first £50,000; and (iii) for insurance, 100 per cent. where claims arise (a) in respect of a liability subject to compulsory insurance; (b) in respect of a liability subject to professional indemnity insurance; and (c) from the death or in capacity of the policy holder due to injury, sickness or infirmity; 90% of the claim where claims arise under other types of policy with no upper limit (for claims against firms declared in default on or after 3 July 2015).

The FSCS only pays compensation for financial loss. Compensation limits are per person, per firm and per type of claim. These limits reflect Directive 2009/14/EC, amending Directive 94/19/EC on deposit guarantee schemes (the **DGSD**) which requires Member States to set the minimum level of

compensation for deposits, for firms declared in default on or after 1 January 2011, at €100,000. A review of the DGSD has been completed and the recast DGSD 2014/49/EC, strengthening the protection of citizens' deposits in case of bank failures, was published in the Official Journal on 12 June 2014. Implementation by EU member states was required by July 2015. The description of the FSCS above reflects, so far as relevant, the UK implementation of the recast DGSD.

## **2.9 Financial Ombudsman Service**

The Financial Services and Markets Act 2000 established the Financial Ombudsman Service (the **FOS**), which determines complaints by eligible complainants in relation to authorised financial services firms, consumer credit licensees and certain other businesses, in respect of activities and transactions under its jurisdiction. The FOS determines complaints on the basis of what, in its opinion, is fair and reasonable in all the circumstances of the case. The maximum level of money award by the FOS for complaints received on or after 1 January 2012 is £150,000 excluding interest and costs. The FOS may also make directions awards, which direct the business to take steps as the FOS considers just and appropriate.

## **2.10 Unfair Terms in Consumer Contracts Regulations 1994 and 1999 and Consumer Rights Act 2015**

In the UK, the Unfair Terms in Consumer Contracts Regulations 1999 as amended (the **1999 Regulations**), together with (in so far as applicable) the Unfair Terms in Consumer Contracts Regulations 1994 (together with the 1999 Regulations, the **UTCCR**), apply to agreements made on or after 1 July 1995 and before 1 October 2015. The UTCCR provides that a consumer may challenge a standard term which has not been individually negotiated in an agreement on the basis that it is “unfair” within the UTCCR and therefore not binding on the consumer (although the rest of the agreement will remain enforceable if it is capable of continuing in existence without the unfair term), and the lead enforcement body, and any “qualifying body” within the UTCCR (such as the FCA), may seek to enjoin a business from relying on unfair terms.

The UTCCR will not generally affect terms which define the main subject matter of the contract, such as the borrower's obligation to repay the principal, or price terms, provided that these terms are written in plain and intelligible language and are drawn adequately to the consumer's attention. The UTCCR may affect terms that are not considered to be terms which define the main subject matter of the contract or price terms, such as the lender's power to vary the interest rate and certain terms imposing early repayment charges and mortgage exit administration fees. For example, if a term permitting the lender to vary the interest rate (as the originator is permitted to do) is found to be unfair, the borrower will not be liable to pay interest at the increased rate or, to the extent that the borrower has paid it, will be able, as against the lender, or any assignee, to claim repayment of the extra interest amounts paid or to set off the amount of the claim against the amount owing by the borrower under the loan or any other loan agreement that the borrower has taken with the lender (or exercise analogous rights in Scotland).

Responsibility for enforcing the UTCCR and the Consumer Rights Act 2015 (the **CRA**) is divided between the CMA and certain other regulatory bodies, with the CMA being the lead regulator. Prior to 1 April 2014, the lead regulator for enforcement of the UTCCR was the Office of Fair Trading. The FCA has powers to enforce the UTCCR and the CRA in relation to agreements concerning financial services and products, including mortgages and other consumer credit agreements. While the CMA and FCA have powers to enforce the UTCCR and the CRA, it would be for a court to determine their proper interpretation. The extremely broad and general wording of the UTCCR makes any assessment of the fairness of terms largely subjective and makes it difficult to predict whether or not a term would be held by a court to be unfair. It is therefore possible that any loans covered by the UTCCR may contain unfair terms which may result in the possible unenforceability of the terms of the underlying loans.



The CRA, which came into force from an unfair contract terms perspective on 1 October 2015 (the **CRA Commencement Date**), provides that, among other things, a term which specifies the main subject matter of the contract, or a price term, is exempt from being reviewed as to its fairness if the term is transparent and prominent and that, in proceedings brought by individual consumers, the court is required to consider the fairness of a term, even if the consumer has not raised the issue of unfairness, where the court has available to it the legal and factual elements necessary for that task.

The CRA reforms and consolidates consumer law in the UK. The CRA involves the creation of a single regime for unfair contract terms out of the Unfair Contract Terms Act 1977 (the **UCTA**) (which essentially deals with attempts to limit liability for breach of contract) and the UTCCR. On the CRA Commencement Date, certain sections of the CRA revoked the UTCCR, and introduced a new regime for dealing with unfair contractual terms with respect to contracts entered into on or after the CRA Commencement Date. The UTCCR will continue to apply to contracts entered into prior to the CRA Commencement Date as described above.

Under Part 2 of the CRA an unfair term of a consumer contract (a contract between a trader and a consumer) is not binding on a consumer (a term which has been revised to mean an individual acting for purposes that are wholly or mainly outside that individual's trade, business, craft or profession). In an additional change from the old regime, from the CRA Commencement Date, an unfair consumer notice will also not be binding on a consumer, although a consumer may rely on the term or notice if the consumer chooses to do so. A term will be unfair where, contrary to the requirement of good faith, it causes significant imbalance in the parties' rights and obligations under the contract to the detriment of the consumer. In determining whether a term is fair it is necessary to: (i) take into account the nature of the subject matter of the contract; (ii) refer to all the circumstances existing when the term was agreed; and (iii) refer to all of the other terms of the contract or any other contract on which it depends. The CRA also applies substantially the same test of fairness to consumer notices and generally refers to term and notices interchangeably.

Schedule 2 contains an indicative and non-exhaustive "grey list" of terms of consumer contracts that may be regarded as unfair. Three of these "grey list" terms are new, having not been covered by the UTCCR. Paragraph 11 lists "a term which has the object or effect of enabling the trader to alter the terms of the contract unilaterally without a valid reason which is specified in the contract". Schedule 2 of the UTCCR contains a substantially similar provision at paragraph 1(j). Although paragraph 22 of the CRA (and paragraph 2(b) of Schedule 2 to the UTCCR) provides that this does not include a term by which a supplier of financial services reserves the right to alter the rate of interest payable by or due to the consumer, or the amount of other charges for financial services without notice where there is a valid reason if the supplier is required to inform the consumer of the alteration at the earliest opportunity and the consumer is free to dissolve the contract immediately.

A consumer contract may not be assessed for fairness to the extent that (i) it specifies the main subject matter of the contract; and/or (ii) the assessment is of the appropriateness of the price payable under the contract by comparison with the goods, digital content or services supplied under it; unless it appears on the "grey list" referenced above. A trader must ensure that a written term of a consumer contract, or a consumer notice in writing, is transparent i.e. that it is expressed in plain and intelligible language and is legible. Under the CRA, a trader must also ensure that the term is sufficiently prominent. The CMA considers this to be fully consistent with an interpretation of 'the core exemption' as intended to ensure that only those 'principal obligations' or price terms which are subject to the correcting forces of competition and genuine decision-making are fully assessable for fairness.

Where a term of a consumer contract is "unfair", it will not bind the consumer. However, the remainder of the contract will, so far as practicable, continue to have effect in every other respect. Where a term in a consumer contract is susceptible of multiple different meanings, the meaning most favourable to the consumer will prevail. In a shift from the old regime, under the CRA it is the duty of the court to consider the fairness of any given term. This can be done even where neither of the parties to proceedings has explicitly raised the issue of fairness.

The provisions in the CRA governing unfair contractual terms apply in respect of contracts entered into on or after the CRA Commencement Date. As stated above, UCTA and UTCCR will continue to apply to contracts entered into prior to the CRA Commencement Date. This new regime does not seem to be significantly different from the regime under the UTCCR and UCTA. However, this area of law is rapidly developing and new regulatory guidance and case law as a result of this new legislation can be expected. No assurance can be given that any changes in legislation, guidance or case law on unfair terms will not have a material adverse effect on the loans.

## **2.11 Distance Marketing**

In the UK, the Financial Services (Distance Marketing) Regulations 2004 apply to, inter alia, credit agreements entered into on or after 31 October 2004 by means of distance communication (i.e. without any simultaneous physical presence of the originator and the borrower). A regulated mortgage contract under the FSMA, if originated by a UK lender from an establishment in the UK, will not be cancellable under these regulations but will be subject to related pre-contract disclosure requirements in MCOB. Certain other credit agreements will be cancellable under these regulations if the borrower does not receive the prescribed information at the prescribed time, or in any event for certain unsecured lending. Where the credit agreement is cancellable under these regulations, the borrower may send notice of cancellation at any time before the end of the 14th day after the day on which the cancellable agreement is made, where all the prescribed information has been received or, if later, the borrower receives the last of the prescribed information.

If the borrower cancels the credit agreement under these regulations, then:

- (a) the borrower is liable to repay the principal, and any other sums paid by the originator to the borrower under or in relation to the cancelled agreement, within 30 days beginning with the day of the borrower sending the notice of cancellation or, if later, the originator receiving notice of cancellation;
- (b) the borrower is liable to pay interest, or any early repayment charge or other charge for credit under the cancelled agreement, only if the borrower received certain prescribed information at the prescribed time and if other conditions are met; and
- (c) any security is treated as never having had effect for the cancelled agreement.

If a significant portion of the loans are characterised as being cancellable under these regulations, then there could be an adverse effect on its receipts in respect of those loans.

## **2.12 Consumer Protection from Unfair Trading Regulations 2008**

On 11 May 2005, the European Parliament and the Council of the EU adopted a Directive (2005/29/EC) regarding unfair business-to-consumer commercial practices (the **Unfair Practices Directive**). Generally, this directive applies full harmonisation, which means that EU member states may not impose more stringent provisions in the fields to which full harmonisation applies. By way of exception, the Unfair Practices Directive permits member states to impose more stringent provisions in the fields of financial services and immovable property, such as mortgage loans. The Unfair Practices Directive provides that enforcement bodies may take administrative action or legal proceedings against a commercial practice on the basis that it is “unfair” within the Unfair Practices Directive.

The Unfair Practices Directive is implemented into UK law by the Consumer Protection from Unfair Trading Regulations 2008 (the **CPUTR**), which came into force on 26 May 2008. The CPUTR prohibit certain practices which are deemed “unfair” within the terms of the CPUTR. Breach of the CPUTR does not (of itself) render an agreement void or unenforceable, but is a criminal offence punishable by a fine and/or imprisonment. The possible liabilities for misrepresentation or breach of contract in relation to the underlying credit agreements may result in irrecoverable losses on amounts to

which such agreements apply. The CPUTR did not initially provide consumers with a private act of redress. Instead, consumers had to rely on existing private law remedies based on the law of misrepresentation and duress. However, amendments to the CPUTR which entered into force on 1 October 2014 have given consumers a right to redress for certain prohibited practices, including a right to unwind agreements.

In addition, the Unfair Practices Directive is taken into account in reviewing rules under the FSMA. For example, MCOB rules for regulated mortgage contracts from 25 June 2010 prevent the lender from (a) repossessing the mortgaged property unless all other reasonable attempts to resolve the position have failed, which include considering whether it is appropriate to offer an extension of term, or conversion to interest-only for a period, or an alternative product, and (b) automatically capitalising a payment shortfall.

## 2.13 Other relevant legislation and regulation

The EU anti-money laundering regime was amended by the implementation of the EU Third Money Laundering Directive (Directive 2005/60/EC) (the **EU Third Money Laundering Directive**), which has imposed requirements in relation to such matters. As a result of the implementation of the EU Third Money Laundering Directive in the UK, the UK Money Laundering Regulations 2007 place a requirement on the Society to identify and verify the identity and address of customers opening accounts with it, and to keep records to help prevent money laundering and fraud. Guidance in respect of the Money Laundering Regulations 2007 is contained in the Guidance Notes of the Joint Money Laundering Steering Group, including in respect of the identification of new clients, record keeping and otherwise. The European Commission published on 5 February 2013 two legislative proposals in relation to the EU anti-money laundering regime: (i) a directive on the prevention of the use of the financial system for the purpose of money laundering and terrorist financing (i.e. the **EU Fourth Money Laundering Directive**); and (ii) a regulation on information accompanying transfers of funds to secure “due traceability” of these transfers (the **Fund Transfer Regulation**). The EU Fourth Money Laundering Directive entered into force on 25 June 2015 and is to be implemented by 26 June 2017. The EU Fourth Money Laundering Directive aims to give effect to the updated Financial Action Task Force standards. It introduces a number of new requirements on relevant businesses and changes to some of the obligations found under the EU Third Money Laundering Directive. The government enacted the Money Laundering Regulations 2017 on 26 June 2017 which implement the EU Fourth Money Laundering Directive and replace the Money Laundering Regulations 2007. The Fund Transfer Regulation updates the rules regarding information on payers and payees accompanying transfers of funds, in any currency, for the purposes of preventing, detecting and investigating money laundering and terrorist financing (**ML/TF**), where at least one of the payment service providers involved in the transfer of funds is established in the EU. The overall objective of transposition is to ensure that the UK’s anti-money laundering and counter terrorist financing (**AML/CTF**) regime is kept up to date, is effective and is proportionate. This will enable the UK to have a comprehensive AML/CTF regime and ensure that the UK’s financial system is an increasingly hostile environment for ML/TF.

The UK Data Protection Act 1998 regulates the processing of data relating to individual customers (which will be replaced on 25 May 2018 by Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data, and repealing Directive 95/46/EC (General Data Protection Regulation)).

The Society participates in the unclaimed assets scheme established under the Dormant Bank and Building Society Accounts Act 2008. The purpose of this scheme is to enable money in dormant bank and building society accounts (i.e. balances in accounts that have been inactive or dormant for 15 years or more) to be distributed for the benefit of the community, while protecting the rights of customers to reclaim their money.

On 1 November 2009, the FSA introduced its Banking Conduct Regime for retail banking. The main constituents of this regime are: (i) extending the FCA's Principles for Businesses as they apply to deposit-taking, from prudential matters only, to conduct of business matters in addition; (ii) conduct of business requirements in the Payment Services Regulations 2009 (the **PSR**), which apply to certain payment services made in euro or sterling; and (iii) the FCA's Banking: Conduct of Business Sourcebook, which applies to deposit-taking in respects not covered by the PSR. The revised directive on payment services (**PSD2**) came into force on 12 January 2016 and was transposed into UK law on 13 January 2018 by the Payment Services Regulations 2017 which repeal and replace the PSR.

On 1 November 2009, the British Bankers' Association, the Building Societies Association and The UK Cards Association launched The Lending Code, a voluntary code on unsecured lending to personal and small business customers, which is monitored and enforced by the Lending Standards Board. The voluntary Banking Code and the Business Banking Code then ceased to have effect. The Lending Code has been revised a number of times since its introduction, most recently in September 2015. Whilst the sections of the Lending Code applicable to micro-businesses remain unchanged, in respect of personal customers the Lending Code was replaced by the Standards of Lending Practice (SLP) in July 2016. The SLP will apply to business customers from 1 July 2017. The SLP are voluntary and set the benchmark for good lending practice in the UK.

Supervisory Statement SS20/15 on supervising building societies' treasury and lending activities sets out the PRA's expectations in respect of building societies' compliance with applicable law and regulation in these areas of activity. The Supervisory Statement was updated on 23 January 2017 and describes the key lending and treasury risks to which societies are exposed, and sets out a framework describing different potential models for managing and controlling these risks.

In September 2016, following a consultation by the PRA earlier that year, the PRA published Policy Statement PS 28/16 and a final Supervisory Statement SS 13/16 both entitled "Underwriting standards for buy-to-let mortgage contracts". The Policy Statement applies to all PRA regulated firms that undertake buy-to let lending that are not already subject to FCA regulation. The Supervisory Statement does not apply to regulated mortgage contracts, consumer buy-to-let mortgages, but-to-let mortgages with corporates or which has a term of 12 months or less or to an application from an existing customer for consent to let. The Supervisory Statement contains the PRA's minimum standards that firms should follow when underwriting buy-to-let mortgages (affordability testing) (including when dealing with portfolio landlords who have four or more buy-to-let properties), clarifies the PRA's expectation regarding the application of the small and medium sized (**SME**) supporting factor on buy-to-let mortgages and details the PRA's expectations regarding adequate risk management and controls. The PRA expects that regulated firms ensure that the standards are followed by other firms undertaking buy-to-lending within their group. The standards were implemented on a phased basis with all standards implemented by 30 September 2017.

#### ***Potential effects of any additional regulatory changes***

No assurance can be given that additional regulatory changes by the CMA, the FCA, the PRA, the FOS or any other regulatory authority will not arise with regard to the financial services market in the UK generally, the Society's particular sector in that market or specifically in relation to it. Any such action or developments or compliance costs may have a material adverse effect on the Society and its respective businesses and operations.

## PART XXI – TAXATION

### 1. UNITED KINGDOM TAXATION

The following statements are intended only as a general guide to certain limited UK tax considerations and do not purport to be a complete analysis of all potential UK tax consequences of acquiring, holding or disposing of Securities. They are based on current UK tax law and what is understood to be the current published practice of HM Revenue and Customs (HMRC) (which may not be binding on HMRC) as at the date of these Listing Particulars, both of which are subject to change at any time, possibly with retrospective effect, which may result in UK tax consequences different from those described below.

The following statements relate only to holders of Securities who are resident (and, in the case of individuals, domiciled) for tax purposes in (and only in) the UK for UK tax purposes, who hold their Securities as an investment and who are the absolute beneficial owner of both the Securities and any Distribution or interest (as applicable) paid on them. References to “interest” refer to interest as that term is understood for United Kingdom tax purposes. The tax position of other categories of Security holders who are subject to special rules (for example (but not limited to), persons acquiring (or deemed to acquire) their Securities in connection with an office or employment, traders, brokers, dealers in securities, insurance companies, banks, financial institutions, tax-exempt organisations and persons connected with or employed by the Society) are not considered.

Prospective investors who are in any doubt as to their tax position or who may be subject to tax in a jurisdiction other than the UK are strongly recommended to consult their own professional advisers.

#### 1.1 Taxation of CCDS

##### (a) Taxation of Distributions

The Society will not be required to withhold UK tax at source from Distributions paid on the CCDS.

##### *Individuals*

An individual CCDS holder who is resident and domiciled for tax purposes in the UK and who receives a Distribution from the Society will, for the tax year from 6 April 2017, pay a nil rate of tax on the first £5,000 of dividend income received in a tax year (the **Nil Rate Amount**). For these purposes “dividend income” includes UK and non-UK source dividends and certain other distributions in respect of shares (including a Distribution from the Society). The rates of tax on dividend income received by such an individual holder of CCDS in excess of the Nil Rate Amount are, for the tax year 6 April 2017 to 5 April 2018: (a) 7.5 per cent. for dividend income within the basic rate tax band; (b) 32.5 per cent. for dividend income within the higher rate tax band; and (c) 38.1 per cent. for dividend income within the additional rate tax band.

Dividend income that is within the Nil Rate Amount counts towards an individual’s basic or higher rate limits, and will therefore potentially affect the level of savings allowance to which they are entitled, and the rate of tax that is due on any dividend income in excess of the Nil Rate Amount. In calculating into which tax band any dividend income over the Nil Rate Amount falls, savings and dividend income are treated as the highest part of an individual’s income. Where an individual has both savings and dividend income, the dividend income is treated as the top slice of an individual’s income. The Nil Rate Amount will be reduced from £5,000 to £2,000 from 6 April 2018.

## *Companies*

CCDS holders within the charge to UK corporation tax which are “small companies” for the purposes of Chapter 2 of Part 9A of the Corporation Tax Act 2009 should not be subject to UK corporation tax on any Distribution received from the Society provided certain conditions are met (including an anti-avoidance condition).

Other CCDS holders within the charge to UK corporation tax will not be subject to UK corporation tax on Distributions received from the Society so long as the Distributions fall within an exempt class and certain conditions are met. However, the exemptions are not comprehensive and are subject to anti-avoidance rules and other conditions.

If the conditions for exemption are not met or cease to be satisfied, the CCDS holder will be subject to UK corporation tax on Distributions received from the Society, at the rate of corporation tax applicable to that CCDS holder for the relevant accounting period (currently 19 per cent. from 1 April 2017, reducing to 17 per cent. from 1 April 2020).

### **(b) Taxation of disposals**

Broadly, for the purpose of UK tax on chargeable gains, the amounts paid by a holder for CCDS will generally constitute the base cost of his holdings in those CCDS.

A disposal or deemed disposal of CCDS by a holder who is resident in the UK for tax purposes may, depending on the holder’s circumstances and subject to any available exemption or relief, give rise to a chargeable gain or an allowable loss for the purposes of UK taxation of chargeable gains.

For UK resident individual holders of CCDS, the principal factors that will determine the UK capital gains tax position on a disposal or deemed disposal of the CCDS are the extent to which the holder realises any other capital gains in the UK tax year in which the disposal is made, the extent to which the holder has incurred capital losses in that or earlier UK tax years, the income tax band to which the holder belongs, and the level of the annual allowance of tax-free gains in that UK tax year (the **Annual Exempt Amount**). For the tax year from 6 April 2017 to 5 April 2018, an individual who is resident in the UK for tax purposes is entitled to an Annual Exempt Amount of £11,300 without being liable to capital gains tax. Any chargeable gain in excess of the Annual Exempt Amount is subject to capital gains tax at 10 per cent. for individuals within the basic rate tax band and 20 per cent. for individuals within the higher or additional rate tax bands.

A UK resident corporate holder within the charge to UK corporation tax should be entitled to claim an indexation allowance to reduce the amount of chargeable gain realised on a disposal. Indexation allowance cannot create or increase an allowable loss. UK corporation tax is charged on chargeable gains at the rate applicable to that company (currently 19 per cent. from 1 April 2017, reducing to 17 per cent. from 1 April 2020). The UK Government announced in its Autumn Budget in November 2017 its intention to freeze indexation allowance with effect from 1 January 2018 and, accordingly, if the UK Government’s proposal is implemented, any indexation allowance would be limited to periods prior to 1 January 2018. UK holders should note that this proposal has not been enacted and may therefore be subject to change.

A holder who is not resident in the UK for tax purposes is generally not subject to UK capital gains tax, unless such a holder carries on a trade, profession or vocation in the UK through a branch or agency or, in the case of a non-UK resident corporate holder, a permanent establishment to which the holding of CCDS is attributable.

Generally, an individual who acquires his or her CCDS while resident, or ordinarily resident in the UK for tax purposes, but who subsequently ceases to be UK resident for a period of 5 years or less and who disposes of his or her CCDS during that period may be liable, on his or her return to the UK, to UK

capital gains tax on any chargeable gain realised on the disposal (subject to any available exemption or relief). Special rules may apply to holders who are subject to tax on a “split-year” basis and such holders should seek specific professional advice if they are in any doubt as to their position.

**(c) Stamp duty and Stamp Duty Reserve Tax (SDRT)**

Following recent case law, no stamp duty or SDRT should be payable in the UK on the issue of the CCDS into the Clearing Systems. Provided no election is or has been made under section 97A of the Finance Act 1986 (a **97A election**) by a Clearing System that applies to the CCDS, no stamp duty or SDRT should be payable on the transfer of CCDS in that Clearing System, without an instrument of transfer. The Society has received confirmation from each of the Clearing Systems that the CCDS would be admitted to its systems without a 97A election applying to the CCDS. However, if a 97A election were to apply to the CCDS in the future, transfers of the CCDS within the Clearing Systems could, unless an exemption applies, be subject to SDRT at the rate of 0.5 per cent. of the consideration given under the agreement to transfer the CCDS.

If definitive CCDS Certificates are issued, SDRT may be payable on an agreement to transfer the CCDS. SDRT would be payable generally at the rate of 0.5 per cent. of the value of the consideration given under the agreement to transfer the CCDS. This charge to SDRT would be discharged if stamp duty is duly paid (rounded up, if necessary, to the nearest £5) on the instrument transferring CCDS in definitive form (or if it is certified as exempt), within six years of the date of the agreement.

**1.2 Taxation of Tier 2 Notes**

**(a) Payments of interest on the Tier 2 Notes**

Payments of interest on the Tier 2 Notes that does not have a UK source may be made without deduction or withholding on account of UK income tax. If interest paid on the Tier 2 Notes does have a UK source, then payments may be made without deduction or withholding on account of UK income tax in any of the following circumstances.

Payments of interest on the Tier 2 Notes may be made without deduction of or withholding on account of UK income tax provided that the Tier 2 Notes carry a right to interest and the Tier 2 Notes are and continue to be listed on a “recognised stock exchange” within the meaning of section 1005 of the Income Tax Act 2007. The Luxembourg Stock Exchange is a recognised stock exchange. The Tier 2 Notes will satisfy this requirement if they are officially listed in Luxembourg in accordance with provisions corresponding to those generally applicable in EEA states and are admitted to trading on the Luxembourg Stock Exchange. Provided, therefore, that the Tier 2 Notes carry a right to interest and are and remain so listed on a “recognised stock exchange”, interest on the Tier 2 Notes will be payable without deduction of or withholding on account of UK tax.

Payments of interest on Tier 2 Notes may be made without deduction of or withholding on account of United Kingdom income tax if the Tier 2 Notes are “regulatory capital securities”. The Tier 2 Notes will be “regulatory capital securities” if they qualify, or have qualified, as Tier 2 instruments under Article 63 of Commission Regulation (EU) No 575/2013 and form, or have formed, a component of Tier 2 capital for those purposes. This is subject to there being no arrangements the main purpose, or one of the main purposes, of which is to obtain a tax advantage (as defined in section 1139 of the Corporation Tax Act 2010) for any person as a result of the application of the Taxation of Regulatory Capital Securities Regulations 2013 in respect of the Tier 2 Notes.

In other cases, an amount must generally be withheld from payments of interest on the Tier 2 Notes that has a UK source on account of UK income tax at the basic rate (currently 20%), subject to any other available exemptions and reliefs. However, where an applicable double tax treaty provides for a lower rate of withholding tax (or for no tax to be withheld) in relation to a holder of Tier 2 Notes,

HMRC can issue a notice to the Society to pay interest to that holder without deduction of tax (or for interest to be paid with tax deducted at the rate provided for in the relevant double tax treaty).

**(b) Further UK tax issues on the Tier 2 Notes**

Interest on the Notes that constitutes UK source income for tax purposes may, as such, be subject to income tax by direct assessment even where paid without withholding.

However, interest with a UK source received without deduction or withholding on account of UK tax will not be chargeable to UK tax in the hands of a holder (other than certain trustees) who is not resident for tax purposes in the UK unless that holder carries on a trade, profession or vocation in the UK through a UK branch or agency in connection with which the interest is received or to which the Tier 2 Notes are attributable (and where that holder is a company, unless that holder carries on a trade in the UK through a permanent establishment in connection with which the interest is received or to which the Tier 2 Notes are attributable). There are exemptions for interest received by certain categories of agent (such as some brokers and investment managers). The provisions of an applicable double taxation treaty may also be relevant for such holders.

In general, holders of the Tier 2 Notes which are within the charge to UK corporation tax will be charged to tax as income on all returns, profits or gains on, and fluctuations in value of, the Tier 2 Notes (whether attributable to currency fluctuations or otherwise) broadly in accordance with their statutory accounting treatment.

**(c) Stamp duty and SDRT**

No stamp duty or SDRT is payable on the issue of, the transfer of or an agreement to transfer any Tier 2 Note, if the Tier 2 Notes are “regulatory capital securities” as described in paragraph 1.2(a) above.

**2. THE PROPOSED FINANCIAL TRANSACTIONS TAX (FTT)**

The European Commission has published a proposal (the **Commission’s Proposal**) for a Directive for a common FTT in Belgium, Germany, Estonia, Greece, Spain, France, Italy, Austria, Portugal, Slovenia and Slovakia (the **participating Member States**). However, Estonia has since stated that it will not participate.

The proposed FTT has very broad scope and could, if introduced in its current form, apply to certain dealings in the Securities (including secondary market transactions) in certain circumstances.

Under current proposals the FTT could apply in certain circumstances to persons both within and outside of participating Member States. Generally, it would apply to certain dealings in the Securities where at least one party is a financial institution, and at least one party is established in a participating Member State. A financial institution may be, or be deemed to be, “established” in a participating Member State in a broad range of circumstances, including (a) by transacting with a person established in a participating Member State or (b) where the financial instrument which is subject to the dealings is issued in a participating Member State.

However, the FTT proposal remains subject to negotiation between participating Member States. It may therefore be altered prior to any implementation, the timing of which remains unclear. Additional EU Member States may decide to participate. Prospective holders of Securities are advised to seek their own professional advice in relation to the FTT.

**3. FOREIGN ACCOUNT TAX COMPLIANCE ACT**

Pursuant to certain provisions of the U.S. Internal Revenue Code of 1986, commonly known as FATCA, a **foreign financial institution** may be required to withhold on certain payments it makes



**(foreign passthru payments)** to persons that fail to meet certain certification, reporting, or related requirements. The Society is a foreign financial institution for these purposes. A number of jurisdictions (including the UK) have entered into, or have agreed in substance to, intergovernmental agreements with the United States to implement FATCA (**IGAs**), which modify the way in which FATCA applies in their jurisdictions. Under the provisions of IGAs as currently in effect, a foreign financial institution in an IGA jurisdiction would generally not be required to withhold under FATCA or an IGA from payments that it makes. Certain aspects of the application of the FATCA provisions and IGAs to instruments such as the Securities, including whether withholding would ever be required pursuant to FATCA or an IGA with respect to payments on instruments such as the Securities, are uncertain and may be subject to change. Holders should consult their own tax advisors regarding how these rules may apply to their investment in the Securities. In the event any withholding would be required pursuant to FATCA or an IGA with respect to payments on the Securities, no person will be required to pay additional amounts as a result of the withholding.

## PART XXII – ADDITIONAL INFORMATION

### 1. INCORPORATION, PRINCIPAL OFFICE AND LEI

- 1.1 The principal office of the Society is 2 Providence Place, West Bromwich, UK, B70 8AF (telephone number +44 (0) 345 241 3784).
- 1.2 The principal legislation under which the Society operates is the Building Societies Act 1986, as amended.
- 1.3 The Society's Legal Entity Identifier (**LEI**) is: 45WSBJYVGC91LG3H515.

### 2. CCDS CAPITAL

- 2.1 By a Special Resolution passed on 28 July 2015 the Rules were amended to enable the Society to issue CCDS.
- 2.2 By a resolution of the Board passed on 27 February 2018 and a resolution of a duly authorised committee of the Board passed on 10 April 2018, the Society has approved the issue of 1,288,813 CCDS.
- 2.3 The rights attaching to the CCDS are set out in "*Part IX: Conditions of Issue of the Core Capital Deferred Shares*". Variations to those rights that will apply whilst the CCDS are represented by the Global CCDS Certificate are set out under "*Overview of Provisions Relating to the CCDS While Represented by the Global CCDS Certificate*" in "*Part IX: Conditions of Issue of the Core Capital Deferred Shares*". Save as disclosed in these Listing Particulars:
  - (a) no CCDS or loan capital of the Society or any of its subsidiaries has within the period covered by the Consolidated Historical Financial Statements or the H1 2017/8 Interim Financial Statements incorporated by reference in these Listing Particulars (other than intra-group issues by wholly owned subsidiaries or pursuant to the Offer) been issued or been agreed to be issued fully or partly paid, either for cash or for a consideration other than cash and no such issue is now proposed;
  - (b) no commissions, discounts, brokerages or other special terms have been granted by the Society or any of its subsidiaries within the period covered by the Consolidated Historical Financial Statements or the H1 2017/8 Interim Financial Statements incorporated by reference in these Listing Particulars in connection with the issue or sale of any CCDS or loan capital of any such company; and
  - (c) no CCDS or loan capital of the Society or any of its subsidiaries is under option or agreed, conditionally or unconditionally, to be put under option.
- 2.4 The CCDS have been registered with the International Security Identification Number (ISIN) GB00BYWR8Q80 and Common Code 179627256.

### 3. TIER 2 NOTES

- 3.1 The issue of the Tier 2 Notes was authorised by resolutions of the Board of the Society passed on 27 February 2018 and resolutions of a duly authorised committee of the Board passed on 10 April 2018.
- 3.2 The Tier 2 Notes have been registered with the International Security Identification Number (ISIN) XS1775405795 and Common Code 177540579.

## **4. EXTRACTS FROM THE SOCIETY'S MEMORANDUM AND RULES**

The Society's current Memorandum and Rules comprise the constitution of the Society and certain key provisions have been extracted and set out below. Terms defined in the Rules have the same meanings in these extracts.

### **4.1 Purposes**

The Society's purposes are set out in paragraph 3 of the Memorandum. Its principal purpose is making loans which are secured on residential property and are funded substantially by its members. The other purposes of the Society are:

- (a) to carry on the businesses of banking, investment, insurance and the provision of financial services and facilities;
- (b) to carry on any businesses connected with the provision of housing or other accommodation or the provision of any services relating to housing or other accommodation;
- (c) to carry on any businesses in the fields of information technology, data processing and communications;
- (d) to carry on any businesses involving the provision of goods or other services (whether for consumers or others) or dealing in any property;
- (e) to act as a parent undertaking and investment body and to assist and co-ordinate the activities of any undertakings in which it holds an interest;
- (f) to promote and support community and charitable purposes; and
- (g) to carry on or participate in any business or other activity which, in the opinion of the Board of Directors or any duly authorised Officer or employee of the Society, may conveniently be carried on in connection with any other activity of the Society or for developing, taking advantage of or protecting any of the property or income of the Society or any connected undertaking of the Society or managing any risks associated with the activities of the Society or any connected undertaking of the Society.

### **4.2 Membership**

No Person shall be a Member of the Society unless he is a Shareholding Member or a Borrowing Member or both, and

- (a) "Shareholding Member" means a Person who holds a Share in the Society and, unless the context otherwise requires, includes a Person whose name is entered in the Deferred Shares Register as the holder of a Deferred Share or a fraction of a Deferred Share; and
- (b) "Borrowing Member" means an Individual:
  - (i) who is indebted to the Society in respect of a Loan or a Loan from another building society whose interest in the Loan has, as the result of any amalgamation or transfer of engagements, passed to the Society, or
  - (ii) who is indebted to the Society as mentioned in (i) above and who has taken with the consent of the Society a transfer of any land already in mortgage to the Society, and who shall become a Borrowing Member as from the date the transfer is registered in the records of the Society, or

- (iii) who, on the death or bankruptcy of a Borrowing Member or otherwise on transfer by operation of law becomes entitled to land already in mortgage to the Society and who (being willing to become a Borrowing Member) is accepted by the Society as a Borrowing Member while such Loan shall be outstanding, from the date of acceptance by the Society.

### 4.3 Shares

The power of the Society to raise funds by the issue of Shares shall be exercised, subject to the Rules and the Statutes, by the issue of Shares or classes of Shares as the Board may from time to time in its absolute discretion determine and the Board may decide to discontinue, suspend, limit or resume the issue of any Shares or class of Shares.

Deferred Shares and preferential Shares may be issued on such terms and conditions as the Board may from time to time in its absolute discretion determine, but the Society's liabilities in respect of such Shares immediately following any such issue shall not exceed 25% of the Society's aggregated share, deposit and loan liabilities.

The terms and conditions of issue on which Shares or classes of Shares are to be issued shall be determined by the Society. Different classes of Deferred Shares may be issued on different terms and conditions including as to ranking, distributions, loss absorbency (including permanent or temporary write-down and re-instatement), conversion into Shares or debt and sharing in surplus assets on a winding-up or dissolution of the Society.

Except in relation to Deferred Shares (in respect of which the terms and conditions of issue shall apply) the Society may at any time change the terms on which Shares or any particular class of Shares already issued are held, in the manner and subject to the conditions set out in the terms applying at that time to such Shares or class of Shares. The Society shall notify each Shareholding Member of a change in the terms on which his Shares are held in the manner specified in the terms which apply to those Shares, or, if those terms do not specify (or do not validly specify) the manner in which such changes are to be notified, then by giving personal notice of the change to the Shareholding Member not less than two months before the date on which the change is to take effect.

Except in relation to Deferred Shares (in respect of which the terms and conditions of issue shall apply) if it appears to the Society that any Shareholding Member is suffering from mental disorder or is through mental infirmity arising from disease or age incapable of managing his affairs, any Person appearing to the Society to have the care of such Shareholding Member or the management of his affairs may, with its consent, withdraw the whole or any part of the amount standing to the credit of that Shareholding Member's account but this will be subject to the terms and conditions applying to any Share.

A Shareholding Member may transfer his Deferred Shares to any Person and no fee shall be charged in respect of a transfer of a Deferred Share. A Shareholding Member may transfer all or any of his Deferred Shares in any manner which is permitted by the terms and conditions of issue and is from time to time approved by the Board. A fully-paid Deferred Share shall be free from all liens in respect of liabilities to the Society.

The Board shall have power to implement any procedures as it thinks fit for the transfer of Deferred Shares and for the regulation of those procedures and to permit Deferred Shares to be transferred other than by a written instrument. Nothing in the Rules shall require a Deferred Share to be transferred by a written instrument if the Board has resolved that no such instrument be required.

*A number of provisions in the Rules are expressed to apply to share investments (covering matters such as notice of changes to terms and conditions, withholding repayment, closing accounts and transfer). These provisions, in practice, apply to share investments in the form of UK retail member deposits in*

*share accounts and not to deferred share investments (including CCDS) which are governed by their terms and conditions.*

#### **4.4 General meetings**

The Society shall hold an Annual General Meeting in each Financial Year, at such hour, date and place as the Board shall determine. The Board shall lay before the Members at the Annual General Meeting the Annual Accounts of the Society for the last Financial Year before the date of that meeting, and shall also submit to them a report by the Board (called in the Rules “the Directors’ Report”) on the business of the Society, which Directors’ Report shall include the information required by or under the Statutes. The following provisions relate to special general meetings of the Society.

- (a) All general meetings other than Annual General Meetings shall be called special general meetings.
- (b) The Board may, whenever it thinks fit, convene a special general meeting.
- (c)
  - (i) The Board shall convene a special general meeting on the requisition of not less than 500 Members qualified as below, and specify the meeting as such in the notice calling it. Subject to the provisions of sub-paragraph (ii) below, the requisition shall state the objects of the meeting, and the full text of any resolution which the requisitioners wish to move at the meeting, (neither of which must include the election of a Director or a resolution which, if passed, would purport to interfere with the Directors’ right and duty to manage the affairs of the Society). The requisition shall be signed by the requisitioners and deposited at the Principal Office and may consist of several documents in like form each signed by one or more requisitioners, provided that each document is deposited within 3 months of the date on which the first was deposited. A deposit of £50 in respect of each requisitioner signing the requisition shall be lodged with it. If within half an hour after the time appointed for the meeting a quorum is not present, all such deposits shall be forfeited but if a quorum is present the Members present and entitled to vote at the meeting shall decide by Ordinary Resolution whether the deposits shall be appropriated either wholly or in part towards the expenses of convening and holding the meeting and to any extent to which the deposits are not so appropriated they shall be returned by the Society to the requisitioners equally. If required by the requisition, the Board shall, subject to sub-paragraph (iii) below, send to each Member entitled to receive notice of the meeting a copy of a statement of not more than 500 words with respect to the matters to be dealt with at the meeting.
  - (ii) The Board shall be under no duty to convene such a special general meeting if:
    - (A) the only or main object of the meeting as stated in the requisition is to move a resolution in substantially the same terms as any resolution which has been defeated at a meeting or on a Ballot during the period beginning with the third Annual General Meeting before the date on which the requisition is deposited at the Principal Office, or
    - (B) the date of the meeting would fall during the period of four months beginning one month after the end of the Financial Year.
  - (iii) The Board shall be under no duty to send copies of a statement to Members entitled to receive notice of the meeting in any case where -
    - (A) the statement does not relate directly to the affairs of the Society, or

(B) publicity for the statement would be likely to diminish substantially the confidence in the Society of investing members of the public, or

(C) the rights conferred by paragraph (i) above are being abused to seek needless publicity for defamatory matter or for frivolous or vexatious purposes,

and the Regulator shall hear and determine any dispute arising from sub-paragraph (B) above.

(d) A Member shall be qualified under this paragraph for the purposes of paragraph (c) above if he:

(i) has or had a Shareholding to the value of not less than £100 or owes or owed to the Society a Mortgage Debt of not less than £100 on the qualifying date, and

(ii) had held such a Shareholding or owed such a Mortgage Debt for a continuous period of not less than two years ending with the qualifying date, and

(iii) is not a minor,

and in (i) and (ii) above the “qualifying date” is either the date of deposit of the sole requisition or the date of deposit of the last requisition sufficient to comply with the requirements of paragraph (c).

For the purposes of this paragraph (d), the value of a Deferred Share shall be counted as held by a Member, only if, at the qualifying date, the Member was entered in the Deferred Shares Register as the holder of that Deferred Share.

In addition, to be qualified under this paragraph for the purposes of paragraph (c) above, a Member must:

(i) state his full name and address, and

(ii) identify a share account or holding of Deferred Shares or mortgage account with the Society which will evidence the fact that he fulfils the conditions set out in paragraphs (i) and (ii) above.

If the Board wishes to object to the requisition by virtue of any of the requirements of this paragraph or paragraph (c) above not being met, it must do so within 14 days of the requisition or document being deposited at the Principal Office.

(e) If the Board does not within 28 days after the date of deposit of the sole requisition or the date of deposit of the last requisition sufficient to comply with the requirements of paragraph (c) above proceed to despatch notices convening a meeting to be held within 63 days after that date, the requisitioners or any proportion of them exceeding one-half may themselves convene a special general meeting, but any meeting so convened shall not be held after the expiration of five months from the date of the deposit of the sole or last requisition. The meeting so convened by the requisitioners shall be convened in the same manner, as nearly as possible, as that in which meetings are convened by the Board and notices of it shall be sent to the Persons entitled to it under Rule 32(3).

The Board or, as the case may be, the requisitioners shall give to the Members notice of any resolution the requisitioners propose to move at the meeting at the same time and in the same manner as notice is given of the meeting.

If the Board is required under paragraph (c)(i) above to send a statement to Members entitled to receive notice of the meeting and does not comply with the requirement within 28 days from the date of the deposit of the sole requisition or the date of deposit of the last requisition, not less than one half of the requisitioners themselves may send a copy of the statement to each Member entitled to receive notice of the meeting.

Any days falling within the period mentioned in paragraph (c)(ii)(B) above shall be disregarded in determining any period for the purposes of this paragraph.

Any reasonable expenses incurred by the requisitioners by reason of the failure of the Board duly to convene a meeting shall be paid to those requisitioners by the Society. Any sum so paid shall be recovered by the Society from the defaulting Directors (whether by way of retention of fees or other remuneration in respect of services, or otherwise).

- (f) No business shall be entertained at any special general meeting except such as shall be stated in the notice convening the meeting or, (where applicable), to decide by Ordinary Resolution whether the deposits mentioned in paragraph (c)(i) above shall be appropriated either wholly or in part towards the expenses of convening and holding the meeting.
- (g) Except where the requisitioners themselves convene a special general meeting under paragraph (e) of this Rule, special general meetings shall be held at such hour, date and place as the Board shall determine.
- (h) The accidental omission to give, send or deliver a statement to, or the non-receipt of a statement by, any Person entitled to receive a statement shall not invalidate the proceedings at that meeting.
- (i) A special general meeting may, if the Board so determines, be convened at multiple locations through use of communications equipment which allows all Individuals participating in the meeting to both see and hear each other. An Individual so participating shall be deemed to be present in person at the meeting and shall be entitled to vote or be counted in a quorum accordingly. Such a meeting shall be deemed to take place where the Chairman of the meeting is present.

#### **4.5 Entitlement to propose resolutions**

- (1) For the purposes of the following paragraphs of this Rule the following expressions shall have the following meanings -
  - (a) "Qualified Member" means a Member who has been a Member for not less than two years before the qualifying date, was not a minor on the qualifying date, and either -
    - (i) holds or held Shares to the value of not less than £100 on the qualifying date, or
    - (ii) owes or owed a Mortgage Debt to the Society of an amount not less than £100 on the qualifying date, and
    - (iii) at all times during that period of two years, was such a Shareholding Member or such a Borrowing Member, and in this paragraph the "qualifying date" is the date on which the notice of intention to have the resolution moved is given to the Society. For the purposes of this sub-paragraph (a), the value of a Deferred Share shall be counted as held by a Member, only if, at the qualifying date, the Member was entered in the Deferred Shares Register as the holder of that Deferred Share.
  - (b) "Requisite Number" means 500, and

- (c) "Members' Notice" means a notice given to the Society in writing (whether in one or more documents) by at least the Requisite Number of Qualified Members, of their intention to have moved on their behalf at an Annual General Meeting a resolution that is specified in the notice and is either a Special Resolution or an Ordinary Resolution, but is not a Shareholding Members' Resolution or a Borrowing Members' Resolution.

The notice must :

- (i) be signed by the Members giving the notice;
- (ii) state the full names and addresses of those Members; and
- (iii) identify, in relation to each such Member, a share or mortgage account, or a holding of Deferred Shares, which will evidence the fact that the Member fulfils the conditions set out in sub-paragraph

(a)(i) and (iii) above or (as the case may be) the conditions set out in sub-paragraph (a)(ii) and (iii) above.

If the Board wishes to object to a Members' Notice by virtue of any of the requirements of Rule 33(1)(c)(i) to (iii) not being complied with, it must do so within 14 days of the notice being given to the Society.

- (2) If the Society receives a Members' Notice, (subject to paragraphs (3) and (4) below) the Board shall:
- (a) include in the notice of the Annual General Meeting a notice specifying the intention of those Members moving it to have the resolution moved on their behalf at that meeting and, if applicable, the intention to move it as a Special Resolution; and
  - (b) at the request of the Qualified Members intending to have the resolution moved on their behalf, include in the notice of that meeting to each Member entitled under Rule 32(3) above to receive notice of that meeting a copy of any statement of not more than 500 words with respect to the matter referred to in the resolution.
- (3) The Board shall be under no duty -
- (a) to include a Members' Notice in the notice of the Annual General Meeting, or
  - (b) to send to Members such a statement as is mentioned in paragraph 2(b) above if -
    - (i) the Members' Notice (or the last of the documents sufficient to enable it to comply with the requirements of paragraph 1(c) above) and, if submitted, any statement given (of the kind mentioned in paragraph 2(b) above) are given to or lodged with the Society later than the last day of the Financial Year preceding that in which the Annual General Meeting at which it is intended to move the resolution is held, or
    - (ii) the resolution specified in the Members' Notice and, if lodged, any such statement does not relate directly to the affairs of the Society, or
    - (iii) publicity for the resolution specified in the Members' Notice or, as the case may be, the statement would be likely to diminish substantially the confidence in the Society of investing members of the public, or
    - (iv) the rights conferred by paragraph (2) above are being abused to seek needless publicity for defamatory matter or for frivolous or vexatious purposes, or



- (v) the resolution specified in the Members' Notice is in substantially the same terms as any resolution that has been defeated at a meeting or on a Ballot during the period beginning with the third Annual General Meeting before the date on which the Members' Notice (or the last of the documents sufficient to enable it to comply with the requirements of paragraph 1(c) above) is given to the Society, or
  - (vi) the resolution if passed would purport to interfere with the Directors' right and duty to manage the affairs of the Society, and the Regulator shall hear and determine any dispute arising from sub-paragraph (iii) above.
- (4) If it is not practicable for any reason to include a Members' Notice, duly given, within the notice of the Annual General Meeting, the Members' Notice so given together with any statement, duly lodged, as mentioned in paragraph 2(b) above shall be sent along with the notice of that meeting. If, however, that is not practicable, the Members' Notice so given and any statement so lodged shall be sent as soon as practicable after the despatch of the notice of that meeting.

#### **4.6 Entitlement of members to vote on resolutions**

A member may vote on a resolution at a general meeting (or in a postal ballot) if they are a qualified voting member. Subject to satisfying the conditions described below, a Member is entitled to vote -

- (a) on an Ordinary Resolution or a Special Resolution if he was, at the end of the last Financial Year before the voting date, and is, on the voting date, a Shareholding Member or Borrowing Member,
- (b) on a Shareholding Members' Resolution if he was, at the end of that year, and is, on the voting date, a Shareholding Member, and
- (c) on a Borrowing Members' Resolution if he was, at the end of that year, and is, on the voting date, a Borrowing Member.

A Shareholding Member is entitled to vote on a resolution (whether Ordinary, Special or Shareholding Members') if -

- (i) being an Individual they are not a minor on the voting date or, where they are voting by proxy, on the date of the meeting at which the resolution is intended to be moved, and
- (ii) in the case of a joint Shareholding they are the Representative Joint Shareholder, and
- (iii) held he held Shares to the value of not less than £100 -
  - (A) at the end of the Financial Year before the voting date, or
  - (B) if the voting date falls during that part of the Financial Year which follows the conclusion of the Annual General Meeting commenced in that year, at the beginning of the period of 56 days immediately preceding the voting date for Members voting in person at a special general meeting or a Ballot,

as the case may be, and

- (iv) he has not ceased to hold Shares at any time between the time referred to above (as applicable) and the voting date,

and for these purposes, the value of a Deferred Share shall be counted as held by a Member only if at the end of the Financial Year before the voting date or at the beginning of the period of 56 days

immediately preceding the voting date (as applicable), the Member was entered in the Deferred Shares Register as the holder of that Deferred Share.

To vote as a Borrowing Member, a Member must have owed at least £100 on a mortgage loan both at the end of the financial year before the voting date and on the voting date and must not be a minor on the date of the meeting.

For these purposes, the voting date is the date of the meeting at which the resolution is intended to be moved, or in the case of a Member appointing a proxy to vote instead of him at a meeting, the date the Society specifies as the final date for the receipt of instruments appointing proxies to vote on that resolution.

A qualified voting member is entitled to one vote irrespective of the number and value of his share investments and mortgage loans.

Any resolution shall be passed as an Ordinary Resolution (which requires a simple majority of votes cast) unless the Rules of the Society or the Act (including any orders made under it) require otherwise.

#### **4.7 The Board of Directors**

The business of the Society and any business that the Society proposes to carry on shall be under the direction of a Board of Directors consisting of not more than fifteen nor (subject to the provisions of Rule 25(6)) less than five Members and the Board may from time to time resolve the number who together shall constitute the Board within these limitations.

The Board may exercise all those powers of the Society that are not, by the Statutes or by the Rules, required to be exercised by the Society in general meeting.

Each Director must hold a share investment to a value of not less than £1,000.

#### **4.8 Board meetings**

The Board shall meet for the despatch of business as often as it shall find necessary. A Director may, and the Secretary at the request of a Director shall, call a meeting of the Board. A quorum is formed when there are five Directors present.

Questions arising at a meeting are resolved by a majority of votes and, in the case of an equality of votes, the Chairman of the meeting shall have a second or casting vote.

All acts done by the Board, or any committee, or any local board, shall be valid even though it might afterwards be discovered that there was some defect in the constitution of the Board, or committee, or local board, or in the election, or re-election, or appointment, of any member of the Board, or committee, or local board, or Individual acting as such. Likewise, such acts shall not be invalidated by reason of the fact that any Individual acting in such capacity was disqualified from holding office, or was not entitled to vote.

A resolution in writing signed by all the members of the Board or of a committee of Directors or any local board shall be as valid and effectual as if it had been passed at a meeting of the Board or (as the case may be) a committee of Directors or any local board duly convened, constituted and held and may consist of several documents (which may be or include Electronic Communications) in a like form each signed by one or more Directors or (as the case may be) members of the local board.

#### **4.9 Appointment, election and retirement of Directors**

At its first meeting after every Annual General Meeting the Board shall elect from its number a Chairman and a Deputy Chairman who shall hold office until the commencement of the first meeting of the Board held after the next Annual General Meeting unless either shall cease in the meantime to be a Director or shall resign the office. The Chairman shall preside at all meetings of the Board at which he is present and in the absence of the Chairman the Deputy Chairman shall take his place.

Elections of Directors shall be conducted either on a poll taken at the Annual General Meeting or, if the Board so determines, by Ballot of the Members conducted during that part of the Financial Year which precedes the date of the Annual General Meeting. If an election is conducted by Ballot the following provisions of this Rule shall apply to the Ballot by making any necessary consequential amendments.

Where Directors are to be elected at the Annual General Meeting, a form for the appointment of a proxy shall be sent to each Person entitled to notice of the meeting. Subject to compliance additional requirements in certain circumstances, the vacancies shall be filled by those candidates obtaining the most votes in their favour. The Persons entitled to vote in an election of Directors are those Members who, on the voting date, are entitled to vote on an Ordinary Resolution.

The following provisions of the Rules shall apply to the poll -

- (a) the voting papers shall include the number of vacancies on the Board, the full names of all the candidates and any declarations required by the Statutes,
- (b) subject to paragraph (a) above, the Board may prescribe or approve the form of the voting paper (which may be made available and completed by means of Electronic Communication) as permitted by the Statutes and may include such other declarations and denoting of retiring Directors as it thinks fit,
- (c) the voting shall be effected by the placing of an 'X' after the names of the candidates for whom the votes are to be cast, or by such other method of identification as approved by the Board and which is permitted by the Statutes,
- (d) the voting paper shall be void if a Member votes for more candidates than there are vacancies to be filled.

In addition to any Director retiring and any Director choosing to retire and stand for re-election, the other Directors who have not been elected or re-elected at either of the last two Annual General Meetings shall retire from office at the Annual General Meeting each year.

In the case of any vacancy not occasioned by the retirement of any Director by rotation the Board may at any time, and from time to time, appoint an Individual as a Director to fill such vacancy. A Director appointed under this Rule shall hold office until the conclusion of the Annual General Meeting next following such appointment but, if he is appointed on a date falling within a period commencing with the beginning of the Financial Year and ending with the Annual General Meeting held in that year, he shall (unless otherwise determined by the Board) not retire at that Annual General Meeting but -

- (a) at the conclusion of the next Annual General Meeting, or
- (b) at the expiration of the period of 16 months beginning with the date of his appointment,

whichever is the earlier.

#### **4.10 Remuneration of Directors**

The annual remuneration of the Directors as members of the Board (exclusive of any remuneration paid in respect of executive duties) shall be paid at a rate to be determined by the Board from time to time but not exceeding three pence per one hundred pounds of total assets of the Society as at the first day of the Financial Year in which payment is made. This remuneration shall be divisible among the Directors in such proportion as may be agreed among them by a majority decision and, in default of agreement, in equal shares.

In addition to such remuneration, any Director may be paid such reasonable travelling, accommodation and other expenses as he might incur while attending Society business with the approval of the Board. He may also, by resolution of the Board, be paid for professional or other work done by him on behalf of the Society in addition to his usual services as a Director.

#### **4.11 Directors' interests**

A Director may hold any office or place of profit with the Society (other than the office of auditor or valuer) simultaneously with his office of Director and may be appointed by the Board to an office or place of profit with any body corporate in which the Society is, or will be, interested.

A Director so appointed to an office or place of profit with a body corporate in accordance with the paragraph above shall disclose to the Board any benefit he derives from any such office or place in the Financial Year in which it is received.

A Director, notwithstanding his interest, may be counted in the quorum present at any meeting at which he or any other Director is appointed to hold any office or place of profit with the Society or with any body corporate in which the Society is, or will be, interested or at which the terms of any such appointment are arranged. He may vote on any such appointment or arrangement other than his own appointment or the arrangement of the terms of that appointment.

Subject to a Director's complying with the provisions for the time being of the Statutes that –

- (a) require him to declare to the Board any direct or indirect interest he might have, or be treated as having in any contract to which the Society is a party,
- (b) prohibit particular contracts,
- (c) require a contract to be approved by a resolution of a general meeting, or
- (d) require him to furnish to the Society particulars of any related business,

he may enter into or be interested, whether directly or indirectly, in contracts with the Society and shall not be disqualified from office as a result of his interest, nor shall he be liable to account to the Society for any profit arising out of any such contract to which he is a party or in which he is interested by reason of his being at the same time a Director.

Except as otherwise required by the Rules, no Director may vote as a Director in regard to any contract, or proposal for a contract, in which he is interested, whether directly or indirectly, or upon any matter arising out of it. If he shall so vote, his vote shall not be counted nor shall he be reckoned in estimating a quorum when any such contract, or proposal for a contract, is under consideration.

#### **4.12 Directors' indemnity**

Every Director, every other Officer and every employee of the Society shall be indemnified by the Society against any liability in respect of losses, costs, charges, damages and expenses which might

arise from, or in the course of, his duties, but not against any such liability as, by virtue of any rule of law or of the Statutes, would attach to him in respect of any negligence, default, breach of duty or breach of trust of which he might be guilty in relation to the Society. He shall, however, be indemnified against any liability incurred by him in defending any proceedings whatsoever, whether civil or criminal, arising out of his duties in relation to the Society in which judgement is given in his favour or in which he is acquitted.

#### **4.13 Vacation of office and disqualification**

A Director shall cease to hold office:

- (a) if they resign their office by notice in writing to the Secretary on the date specified in the notice or, if none, the date that the notice is received by the Secretary;
- (b) if they cease to hold in their own right a Shareholding of not less than £1,000;
- (c) if they take up a permanent residence outside the United Kingdom;
- (d) if they are requested in writing by a majority of his co-Directors to resign and a resolution that he has vacated office is thereafter passed at a meeting of the Board by at least a majority of the members of the full Board;
- (e) if for more than six consecutive months he absents himself without permission of the Board from meetings of the Board held during that period and the Board passes a resolution that he has vacated office;
- (f) if he becomes bankrupt or is sequestrated or compounds or makes any arrangement with his creditors generally;
- (g) if he is, or might be, suffering from mental disorder and either -
  - (i) he is admitted to hospital in pursuance of an application for admission for treatment under the provisions of the Mental Health Act 1983 or he is admitted to hospital under the provisions of the Mental Health (Scotland) Act 1984 or the provisions of the Mental Health (Northern Ireland) Order 1986, or
  - (ii) an order is made by a court having jurisdiction (whether in the United Kingdom or elsewhere) in matters concerning mental disorder for his detention or for the appointment of a deputy, curator bonis or other Individual to exercise powers with respect to his property or affairs;
- (h) upon a resolution of which notice has been given under Rule 33(2)(a) that he shall cease to be a Director being passed by a majority of the votes cast on a poll at a general meeting;
- (i) if, whilst a Director of the Society and without the consent of the Board, he accepts the office of a director or officer in, or employment by, any other building society or firm which has permission under Part IV of the Financial Services and Markets Act 2000 to accept deposits or enter into regulated mortgage contracts as lender, or any other organisation, company or body deemed by the Board to be in direct competition with the business of the Society;
- (j) if he retires at the conclusion of an Annual General Meeting as a result of any binding requirement of the Statutes regarding retirement of a Director by reason of his age;
- (k) if he becomes prohibited by law from being a Director;

- (l) if he contravenes Rule 21(1) by knowingly or recklessly failing to declare an interest and the Board passes a resolution that he has vacated office;
- (m) in the case of a Director who holds executive office, if his appointment to such office is terminated or expires and the Board resolves that his office be vacated.; or
- (n) if the Board passes a resolution to that effect after either: (1) the Regulator has made it a condition of the Society's continued authorisation that the Director should cease to hold office or has imposed a requirement or made a recommendation that he should cease to hold office; or (2) the Director has failed to obtain or maintain any personal authorisation required from the Regulator relevant to the office of Director.

#### **4.14 Dissolution or winding-up**

Upon the winding-up of the Society, or upon it being dissolved by consent, any surplus remaining after payment in full of the Society's creditors and repayment to Members of the amount of their Shares (together with interest due thereon) according to their priority under their respective terms and conditions of issue (but excluding Core Capital Deferred Shares unless and to the extent provided in their terms and conditions of issue), shall be divided among:

- (a) qualifying Members in proportion to the value of their Shareholding (excluding any Deferred Shares) at the relevant date;
- (b) up to 20% to holders of Deferred Shares (excluding Core Capital Deferred Shares) at the relevant date subject to, and in proportion to the amount specified in, or calculated by reference to, their terms and conditions of issue; and
- (c) holders of Core Capital Deferred Shares at the relevant date subject to, and in proportion to the amount specified in, or calculated by reference to, their terms and conditions of issue.

The relevant date is the earlier of either the date of notice of a winding-up or dissolution resolution or the date of presentation of a winding-up petition or such other date as may be specified by the insolvency official appointed with primary responsibility for the winding-up or dissolution of the Society.

If there are insufficient assets to repay all Members the amounts payable on their Shares in accordance with their terms and conditions of issue, no repayments shall be made in respect of any Deferred Share until after all other Members have been repaid in full.

For the purposes of this Rule, "qualifying Members" means Persons who hold on the relevant date, and have held, throughout the period of two years up to that date, Shares (excluding any holding of Deferred Shares) to the value of not less than £100.

### **5. DEFERRED SHARE CAPITAL OF THE SOCIETY**

As at the date of these Listing Particulars, the Society has two classes of deferred share capital outstanding, namely its PIBS and its PPDS. The Rules also make provision for issue of CCDS.

*LME*

In February 2017, the Society announced that it was seeking clarification from the EBA in relation to the eligibility of its PPDS as CET1 capital, following an investor challenge.

While the Society continues to believe that the PPDS met the CET1 criteria in all respects, the Society in the meantime had constructive engagement with major holders of both the PPDS and the PIBS with

respect to its options. It was clear throughout discussions with these major holders that, irrespective of the outcome of the EBA's deliberations on eligibility of the PPDS, the major holders and the Society were aligned in their views that a modernisation of the Society's capital structure would be appropriate. Following these discussions, the Society announced on 13 December 2017 its plans to conduct the LME involving its PPDS and the PIBS.

The Society launched the LME on 8 March 2018, and announced the final results of the LME on 10 April 2018. The Society expects the LME to settle on 12 April 2018.

As a result of the LME, the Society expects that, following the scheduled settlement date of 12 April 2018 (and in addition to its issuance of Tier 2 Notes), the following changes will have been made to its Deferred Share capital:

- the PPDS will have ceased to be outstanding;
- the nominal amount outstanding of the PIBS will have been reduced to £8,891,000; and
- the Society will have issued 1,288,813 CCDS, corresponding to £128,881,300 at the issue price of £100 per CCDS.

## 6. DIRECTORS

6.1 The biographies of the Directors are set out in "*Part XIII: Directors, Employees and Corporate Governance*".

6.2 The business address of each of the Directors is: 2 Providence Place, West Bromwich, UK, B70 8AF

6.3 In addition to their directorships of the Society, the Directors hold, or have held, the following directorships and are or were members of the following partnerships:

Name	Age	Position	Other directorships and interests
Mark Nicholls	68	Chairman and Non-Executive Director	Northern Investors Company PLC Rathbone Brothers Plc Rathbone Investment Management Ltd
Jonathan Westhoff	53	Chief Executive	West Bromwich Commercial Limited West Bromwich Homes Limited West Bromwich Mortgage Company Ltd CL Mortgages Limited
Mahomed Ashraf Piranie	54	Group Finance & Operations Director	Elite Star Investment Limited Osborne House Property Management Ltd DPC (2011) Limited West Bromwich Mortgage Company Ltd CL Mortgages Limited
Julie Hopes	50	Non-Executive Director	Co-op General Insurance Police Mutual Assurance Society
Mark Preston	58	Non-Executive Director	Acenden Limited Kensington Mortgage Company Ltd
Martin Ritchley	71	Deputy Chairman, Senior Independent Director and Non-Executive Director	Royal Shakespeare Theatre Trust
Richard Sommers	61	Non-Executive Director	Sidmouth Rugby Football Club Limited Al Rayan Bank PLC
Stuart James	48	Non-Executive Director	Prudential Plc

<b>Name</b>	<b>Age</b>	<b>Position</b>	<b>Other directorships and interests</b>
Turner			
Colin Walklin	63	Non-Executive Director	Standard Life Investments (Holdings) Limited Standard Life Investments Limited Standard Life Portfolio Investments Limited Standard Life Wealth Limited Standard Life Overseas Holdings Limited Standard Life Employee Services Limited

6.4 At the date of these Listing Particulars none of the Directors has at any time within at least the past 5 years:

- (a) save as disclosed in this paragraph 6, been a director or partner of any companies or partnerships; or
- (b) had any convictions in relation to fraudulent offences (whether spent or unspent); or
- (c) been adjudged bankrupt or entered into an individual voluntary arrangement; or
- (d) been a director of any company at the time of, or within 12 months preceding, any receivership, compulsory liquidation, creditors voluntary liquidation, administration, company voluntary arrangement or any composition or arrangement with that company's creditors generally or with any class of its creditors; or
- (e) save as disclosed in this paragraph 6, been a partner in a partnership at the time of, or within 12 months preceding, any compulsory liquidation, administration or partnership voluntary arrangement of such partnership; or
- (f) had his assets form the subject of any receivership or been a partner of a partnership at the time of, or within 12 months preceding, any assets thereof being the subject of a receivership; or
- (g) been subject to any official public incrimination and/or sanctions by any statutory or regulatory authority (including any designated professional body); or
- (h) ever been disqualified by a court from acting as a director of a company or from acting in the management or conduct of the affairs of any company.

## **7. DIRECTORS' INTERESTS IN THE SOCIETY**

7.1 None of the Directors nor their immediate families have any interests in the outstanding PPDS or PIBS of the Society, which:

- (a) have or will have been notified to the Society; or
- (b) are interests of a connected person (within the meaning of Schedule 11B of FSMA) which would be required to be disclosed under (a) above and the existence of which is known to or could with reasonable diligence be ascertained by that Director, as at 10 April 2018 (the latest practicable date prior to the publication of these Listing Particulars) nor are expected to have any such interests immediately following Admission.



- 7.2 It is not expected that any Director will have any interest in the CCDS to be issued or loan capital of the Society on Admission and there is no person to whom any capital of any member of the Group is under option or agreed unconditionally to be put under option.
- 7.3 So as the Society is aware, no person has any interest in the Society's capital or voting rights which is notifiable under English law.
- 7.4 The Society is the principal holding entity of the Group and the main business of the Group is conducted by the Society. As a mutual organisation, the Society does not have equity shareholders, and is managed for the benefit of its members, being its current account, retail savings and residential mortgage customers (as well as the holders of its Deferred Shares, including its PIBS, its PPDS and, once issued, its CCDS). In contrast to general meetings of shareholders of a limited company where shareholders may exercise voting rights proportionate to the number of shares they hold, at a general meeting of the members of the Society, each member is entitled to one vote regardless of the size of the member's investment or interest in the Society. Only a member of the Society is entitled to vote at general meetings.
- 7.5 Save as disclosed in "*Part XIII: Directors, Employees and Corporate Governance*", there are no potential conflicts of interest between any duties to the Society (as issuer of the CCDS and the Tier 2 Notes) of the Directors and their private interests or other duties. The Society's governance rules require any conflicts of interest to be disclosed and no Director may vote on a proposal in relation to which he has a conflict.
- 7.6 The Society and the Directors are not aware of any arrangements, the operation of which may at a subsequent date result in a change in control of the Society.

## 8. DIRECTORS' SERVICE AGREEMENTS, BENEFITS AND REMUNERATION

This section provides information on the service agreements and remuneration arrangements for the Executive Directors and Non-Executive Directors.

### 8.1 Executive Directors

#### (a) *Service agreements, remuneration and emolument*

A summary of the terms of the Executive Directors' service agreements with the Society is set out below:

#### **Date appointed to the Board**

Jonathan Westhoff	5 May 2009
Ashraf Piranie	13 March 2017

The following remuneration (including salary, benefits and any contingent or deferred compensation) was awarded to the Executive Directors for services in all capacities in the financial year ended 31 March 2017:

	<b>Basic Salary</b>	<b>Performance- related pay<sup>(1)</sup></b>	<b>Pension</b>	<b>Other benefits<sup>(2)</sup></b>	<b>Total pay</b>
	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>	<b>£'000</b>
Jonathan Westhoff	370	142	93	26	631
Ashraf Piranie	16	-	4	1	21
Mark Gibbard <sup>(3)</sup>	291	126	58	29	504

Notes:

- (1) Included in the amounts shown above is an element that is subject to deferral.
- (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 there are no further payments due to him.

**(b) Termination provisions**

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.

## 8.2 Chairman and Non-Executive Directors

**(a) Service agreements, remuneration and emolument**

Each of the Non-Executive Directors has agreed terms of appointment with the Society as follows:

	<b>Date of Appointment</b>	<b>2016/17 Fees £000</b>	<b>2016/17 Benefits <sup>(1)</sup> £000</b>
Mark Nicholls (Chairman)	01/01/10	120	5
Claire Hafner <sup>(2)</sup>	01/09/11	50	5
Julie Hopes	01/04/16	50	5
Mark Preston	18/05/11	50	4
Martin Ritchley	01/09/09	70	2
Richard Sommers	01/10/09	60	6
Colin Walklin	20/07/11	60	5

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.
- (2) Claire Hafner left the Board in July 2017, with James Turner joining the Board on 1 April 2017.

There is no arrangement under which a Non-Executive Director has waived or agreed to waive future emoluments nor have there been any such waivers during the financial year immediately preceding the date of these Listing Particulars.

**(b) Termination provisions**

The Non-Executive Directors' service agreements make no provision for benefit payable in the event of termination.

## 9. RETIREMENT BENEFIT OBLIGATIONS

Details of the Society's pension schemes are set out in Note 30 to the 2017 Financial Statements.

## 10. SIGNIFICANT SUBSIDIARY AND ASSOCIATED UNDERTAKINGS

The Society has three main subsidiaries; West Bromwich Mortgage Company Limited, West Bromwich Homes Limited and West Bromwich Commercial Limited. The Society holds the interests directly (unless otherwise stated) for key subsidiary undertakings, all of which are registered in England.

The Society's interests in its principal subsidiary undertakings, all of which are consolidated, as at 31 March 2017 are set out below:

Wholly-owned subsidiary undertakings	Nature of business
West Bromwich Mortgage Company Limited	Residential mortgage lending
West Bromwich Commercial Limited	Commercial mortgage lending
CL Mortgages Limited <sup>(1)</sup>	Residential mortgage lending
West Bromwich Homes Limited	Investment in property for rental
Insignia Finance Limited	Second charge lending
White Label Lending <sup>(2)</sup>	Second charge lending

(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.

The Society is the principal holding entity of the Group and the main business of the Group is conducted by the Society.

## 11. 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.

## 12. LITIGATION AND ARBITRATION

Save as disclosed below, there are no governmental, legal or arbitration proceedings which may have or have had in the 12 months prior to the date of these Listing Particulars a significant effect on the financial position or profitability of the Society and/or the Group, nor, so far as the Society is aware, are any such proceedings pending or threatened.

### *PPI*

In its 2017 Financial Statements, the Society made 'Other provisions' in the amount of £1.6 million primarily relating to PPI redress and representing 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*, the 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.

### **13. RELATED PARTY TRANSACTIONS**

Save as disclosed in note 36 to the 2017 Financial Statements, neither the Society nor any other member of the Group has entered into any related party transactions with any related party during the period covered by the Consolidated Historical Financial Statements or H1 2017/8 Interim Financial Statements and up to the latest practicable date prior to publication of these Listing Particulars.

### **14. NO SIGNIFICANT CHANGE AND NO MATERIAL ADVERSE CHANGE**

There has been no significant change in the financial or trading position of the Group since 30 September 2017, the date to which the last interim financial statements of the Society were prepared.

There has been no material adverse change in the prospects of the Society since 31 March 2017, the date of its last published audited financial statements.

### **15. GENERAL**

- 15.1 The total costs and expenses of, and incidental to, the issue of the CCDS and Tier 2 instruments, Admission and the Offer (including professional fees and expenses and the costs of printing and distribution of documents) are estimated to be approximately £2.7 million and are payable by the Society.
- 15.2 The Society is dependent upon its authorisation under the FSMA, with permission to undertake, among other things, deposit-taking, mortgage, and certain consumer credit related, insurance and investment activities. See generally “*Part XX: Supervision and Regulation*”.
- 15.3 Statutory accounts of the Society for each of the financial years ended 31 March 2017, 31 March 2016 and 31 March 2015, which are incorporated by reference in this document, have been prepared and reported on by the Society’s auditor under section 78 of the Act. Each of these auditor’s reports was unqualified and contained no statement under section 79(6) of the Act (failure to obtain necessary information and explanations).

### **16. DOCUMENTS AVAILABLE FOR INSPECTION**

Copies of the following documents are available for inspection during usual business hours on any weekday (Saturdays, Sundays and public holidays excepted) for so long as the Securities are admitted to trading on the Euro MTF at the Society’s registered office at 2 Providence Place, West Bromwich, UK, B70 8AF.

- (a) the existing memorandum and rules of the Society;
- (b) the Consolidated Historical Financial Statements and the H1 2017/8 Interim Financial Statements;
- (c) the December Announcement, the Launch Announcement and the Results Announcement relating to the LME;
- (d) the Consent and Exchange Offer Memorandum;
- (e) the Global CCDS Certificate, Global Tier 2 Certificate and the Agency Agreements; and
- (f) these Listing Particulars.

## PART XXIII – DEFINITIONS

The following definitions apply throughout these Listing Particulars unless the context requires otherwise. Definitions applying to the Conditions of issue of the CCDS and to the Terms and Conditions of the Tier 2 Notes are set out in Condition 17 of “*Part IX: Conditions of Issue of the Core Capital Deferred Shares*” and Condition 18 of “*Part X: - Terms and Conditions of the Tier 2 Notes*” and shall have the same meaning when used elsewhere in these Listing Particulars.

<b>2015 Financial Statements</b>	The Society’s audited consolidated financial statements (including the notes thereto and the audit report in respect thereof) as at, and for the year ended, 31 March 2015, as incorporated by reference in these Listing Particulars.
<b>2016 Financial Statements</b>	The Society’s audited consolidated financial statements (including the notes thereto and the audit report in respect thereof) as at, and for the year ended, 31 March 2016, as incorporated by reference in these Listing Particulars.
<b>2017 Financial Statements</b>	The Society’s audited consolidated financial statements (including the notes thereto and the audit report in respect thereof) as at, and for the year ended, 31 March 2017, as incorporated by reference in these Listing Particulars.
<b>Act</b>	the UK Building Societies Act 1986, as amended.
<b>Admission</b>	admission of the Securities to the Official List of the Luxembourg Stock Exchange and to trading on the Euro MTF Market of the Luxembourg Stock Exchange becoming effective.
<b>ALCo</b>	Assets & Liabilities Committee of the Board.
<b>Authorities</b>	HM Treasury, BoE (including the PRA) and the FCA.
<b>Average Principal Amount</b>	as defined in CCDS Condition 4.5 in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ”
<b>Bank Recovery and Resolution Directive</b>	Directive 2014/59/EU of the European Parliament and of the Council of 15 May 2014 establishing a framework for the recovery and resolution of credit institutions and investment firms.
<b>Banking Act</b>	the Banking Act 2009, as amended.
<b>Banking Consolidation Directive</b>	the Directive of the European Parliament and the Council of 14 June 2006 relating to the taking up and pursuit of the business of credit institutions (No 2006/48/EC).
<b>Banking Reform Act</b>	the Financial Services (Banking Reform) Act 2013.
<b>Basel II</b>	the capital requirements implemented by the EU Capital Requirements Directive, which comprises a Banking Consolidation Directive and a Capital Adequacy Directive implemented in March 2000 and recast in July 2006.
<b>Basel III</b>	a set of reform measures to the regulatory capital framework of the

banking sector issued by the Basel Committee on Banking Supervision on 16 December 2010 and on 13 January 2011, and required to be implemented in Europe over a number of years commencing 1 January 2014.

<b>Basel Committee</b>	the Basel Committee on Banking Supervision.
<b>BoE</b>	the Bank of England.
<b>BRRD</b>	See “Bank Recovery and Resolution Directive” above.
<b>Cap</b>	the prevailing periodic distributions cap on Distributions in respect of the CCDS in respect of any given financial year, determined in accordance with the Rules.
<b>Capital Adequacy Directive</b>	The Directive of the European Parliament and the Council of 14 June 2006 on capital adequacy of investment firms and credit institutions (No 2006/49/ EC).
<b>Capital Disqualification Event</b>	is deemed to have occurred in respect of the Tier 2 Notes if there is a change (which has occurred or which the Supervisory Authority considers to be sufficiently certain) in the regulatory classification of the Tier 2 Notes which becomes effective after the issue date of the Tier 2 Notes and that results, or would be likely to result, in the entire principal amount of the Tier 2 Notes or any part thereof being excluded from the capital of the Society (whether on an individual or consolidated basis).
<b>Capital Requirements Directive and Capital Requirements Regulation</b>	as defined in CCDS Condition 17 in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ” in the definition of Capital Rules.
<b>Capital Rules</b>	as defined in CCDS Condition 17 in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ”.
<b>CCA</b>	Consumer Credit Act 1974
<b>CCDS</b>	the 1,288,813 Core Capital Deferred Shares to be issued by the Society on or around 12 April 2018.
<b>CCDS Agent</b>	Citibank N.A., London Branch as registrar, transfer agent and principal paying agent in relation to the CCDS.
<b>CCDS Conditions</b>	the conditions of issue of the CCDS, as detailed in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ”.
<b>CCDS holder</b>	<ul style="list-style-type: none"> <li>(i) where used in “<i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i>”), has the meaning given in CCDS Condition 17 in “<i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i>”; and</li> <li>(ii) otherwise, means the holder of any CCDS and, where the context admits, may include a person holding a beneficial interest in CCDS through Euroclear or Clearstream, Luxembourg.</li> </ul>

<b>CCDS Register</b>	the records of the Society maintained by the Registrar constituting the register of members for the purposes of the CCDS.
<b>CET1</b>	common equity tier 1 (the highest-quality regulatory capital under the Capital Rules).
<b>Certificates</b>	registered certificates by which the Tier 2 Notes are represented and, save as provided in Tier 2 Condition 1(a), each Certificate shall represent the entire holding of Tier 2 Notes by the same holder.
<b>Clearing Systems</b>	Euroclear, Clearstream, Luxembourg and any successor or replacement clearing systems approved by the Registrar.
<b>Clearstream, Luxembourg</b>	Clearstream Banking S.A.
<b>Closing</b>	the crediting of the Securities to Euroclear and Clearstream, Luxembourg accounts.
<b>CMA</b>	the Competition and Markets Authority
<b>CML</b>	the Council of Mortgage Lenders, which since 1 July 2017 has been integrated into a new trade association, UK Finance.
<b>COBS 22.2</b>	Chapter 22.2 of the Conduct of Business Sourcebook in the FCA's Handbook.
<b>combined buffer</b>	the total Common Equity Tier 1 capital to meet the Society's capital conservation buffer and countercyclical buffer requirements.
<b>Common Equity Tier 1 capital</b>	at any time, has the meaning ascribed thereto (or to any equivalent term) at such time in the Capital Rules.
<b>Compliance Information</b>	such information as the Society (or an agent on its behalf) may from time to time require investors and the intermediaries through which they hold their CCDS to provide to the Society, on a confidential basis, in order for the Society to establish its continued compliance with its obligations under the Luxembourg Rules and such equivalent rules (if any) under the listing rules of any other stock exchange on which the CCDS are, for the time being, listed or admitted to trading.
<b>Conditions</b>	the CCDS Conditions and/or the Tier 2 Conditions, as the context admits.
<b>Consent and Exchange Offer Memorandum</b>	a consent and exchange offer memorandum dated 8 March 2018 prepared by the Society in relation to the Exchange Offers and incorporated by reference in these Listing Particulars.
<b>Consolidated Historical Financial Statements</b>	This consolidated financial statements incorporated by reference into these Listing Particulars, comprising the 2015 Financial Statement, the 2016 Financial Statements and the 2017 Financial Statements.
<b>Conversion Benefits</b>	benefits under the terms of any future transfer of the Society's business to a company, other than rights to receive ordinary shares issued by the successor entity or its parent as specifically provided for under CCDS Condition 10.

<b>Core Capital Contribution Proportion</b>	as defined in CCDS Condition 4.4(b) in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ”.
<b>Core Capital Contribution Share</b>	as defined in CCDS Condition 4.4(a) in “ <i>Part IX: Conditions of Issue of the Core Capital Deferred Shares</i> ”.
<b>CPI</b>	the UK Consumer Price Index.
<b>CRA Regulations</b>	Regulation (EC) No 1060/2009 on credit rating agencies, as amended.
<b>CRD IV</b>	the legislative package comprising the Capital Requirements Directive and the Capital Requirements Regulation.
<b>CRR</b>	the Capital Requirements Regulation.
<b>December Announcement</b>	The announcement made by the Society on 13 December 2017 with respect to its planned LME.
<b>DGSD</b>	EU directive 2014/49/EU on deposit guarantee schemes.
<b>Directors or Board</b>	the Executive and Non-Executive Directors of the Society.
<b>Distributable Items</b>	the aggregate of profits and any reserves of the Society which are available, in accordance with applicable law and regulation for the time being, for payment of Distributions.
<b>Distributions</b>	periodic distributions in respect of the CCDS that may be declared (on an interim and/or final basis) in respect of any financial year in the Board’s sole and absolute discretion/the distributions (if any) from time to time paid to holders of CCDS.
<b>distributor</b>	any person identified as such under MiFID II in connection with the offer, sale or recommendation of any of the Securities.
<b>DPA</b>	Data Protection Act 1998.
<b>EBA</b>	European Banking Authority.
<b>EEA</b>	the European Economic Area.
<b>Euroclear</b>	Euroclear Bank S.A./N.V.
<b>Euro MTF</b>	Euro MTF Market of the Luxembourg Stock Exchange.
<b>Eurozone</b>	the European Monetary Union of those member states of the European Union that have adopted the euro as their common currency and sole legal tender.
<b>Exchange Offers</b>	the invitations by the Society to holders of its existing PIBS and PPDS to offer to exchange their PIBS and/or PPDS for the CCDS, the Tier 2 Notes (in the case of the PPDS only) and cash.
<b>Excluded Dissolution</b>	as defined in Tier 2 Condition 18 in “ <i>Part X: - Terms and Conditions of the Tier 2 Notes</i> ”.



<b>Executive Directors</b>	Jonathan Westhoff Ashraf Piranie	Chief Executive Group Finance & Operations Director
<b>FATCA</b>	the US Foreign Account Tax Compliance Act.	
<b>FCA</b>	the UK Financial Conduct Authority.	
<b>Fitch</b>	Fitch Ratings Limited.	
<b>Financial Performance Framework</b>	the framework that sets out the financial parameters that the Group calibrates future performance against to achieve the right balance between distributing value to members, investing in the business and maintaining its financial strength.	
<b>First Call Date</b>	12 April 2033 (being the first call date for the Tier 2 Notes).	
<b>FLS</b>	the BoE's Funding for Lending Scheme.	
<b>FOS</b>	the UK Financial Ombudsman Service.	
<b>FPC</b>	the Financial Policy Committee	
<b>FS Act</b>	the Financial Services Act 2012.	
<b>FSCS</b>	the Financial Services Compensation Scheme.	
<b>FSMA</b>	the UK Financial Services and Markets Act 2000, as amended.	
<b>Funding for Lending</b>	the BoE's Funding for Lending Scheme.	
<b>FY 2015, FY 2016 and FY 2017</b>	The financial year of the Society ended 31 March 2015, 2016 and 2017, respectively.	
<b>GDPR</b>	the General Data Protection Regulation (Regulation (EU) 2016/679 of the European Parliament and of the Council of 27 April 2016 on the protection of natural persons with regard to the processing of personal data and on the free movement of such data).	
<b>GHOS</b>	the Group of Central Bank Governors and Heads of Supervision, the Basel Committee's oversight body.	
<b>Global CCDS Certificate</b>	the global certificate representing all outstanding CCDS.	
<b>Global Certificates</b>	the Global CCDS Certificate and the Global Tier 2 Certificate.	
<b>Global Tier 2 Certificate</b>	the global certificate representing all outstanding Tier 2 Notes.	
<b>Government</b>	the government of the United Kingdom.	
<b>Group</b>	the Society and its consolidated subsidiaries.	
<b>H1 2017/8 Interim Financial Statements</b>	The Society's unaudited consolidated financial statements as at, and for the 6-month period ended, 30 September 2017, as incorporated by reference in these Listing Particulars.	

<b>IASB</b>	the International Accounting Standards Board.
<b>ICAAP</b>	the Group’s internal capital adequacy assessment process.
<b>ICB</b>	the Government’s Independent Commission on Banking.
<b>IFRS</b>	the international financial reporting standards issued by the IASB, as adopted by the European Commission for use in the European Union.
<b>IMD</b>	Directive 2002/92/EC.
<b>Interest Payment Date</b>	as defined in Tier 2 Condition 5(a) in “ <i>Part X: - Terms and Conditions of the Tier 2 Notes</i> ”.
<b>IRB</b>	internal ratings-based approach to credit risk-weighting.
<b>Issue Price</b>	In respect of the CCDS, £100 per CCDS and, in respect of the Tier 2 Notes, 100 per cent. of their principal amount.
<b>Launch Announcement</b>	The announcement made by the Society on 8 March 2018 launching the LME.
<b>LCR</b>	liquidity coverage ratio.
<b>Listing Particulars</b>	this document.
<b>LMC</b>	Liquidity Management Committee of the Board
<b>LME</b>	The liability management exercise originally announced by the Society on 13 December 2017 and launched on 8 March 2018, pursuant to which eligible holders of PPDS and PIBS were (in the case of professional investors) invited to offer to exchange their PPDS and PIBS for a combination of CCDS, Tier 2 Notes (in the case of the PPDS holders) and cash or (in the case of retail investors holding PIBS) invited to tender their PIBS for purchase by the Society for cash, all as more fully set out in the December Announcement and the Launch Announcement.
<b>LTV</b>	loan to value ratio.
<b>Luxembourg Rules</b>	article 13 of the Grand Ducal Regulation dated 13 July 2007 relating to the holding of an official list for financial instruments and article 702 1.8 of the rules and regulations of the Luxembourg Stock Exchange (version 01/2018), in each case as amended or supplemented or replaced from time to time.
<b>MCOB</b>	the FCA’s Mortgages and Home Finance: Conduct of Business sourcebook
<b>MDA</b>	a maximum distributable amount calculated in accordance with Article 141 of CRD IV.
<b>Memorandum</b>	the memorandum of the Society.
<b>MiFID</b>	the Markets in Financial Instruments Directive (Directive 2004/39/EC)

	of the European Parliament and of the Council of 21 April 2004 on markets in financial instruments the Markets in Financial Instruments Directive).
<b>MiFID II</b>	the revised Markets in Financial Instruments Directive (Directive 2014/65/EU of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments) (and references to MiFID II also include MiFIR where the context admits).
<b>MiFIR</b>	the Markets in Financial Instruments Regulation (Regulation (EU) No 600/2014 of the European Parliament and of the Council of 15 May 2014 on markets in financial instruments).
<b>Minimum Investment Amount</b>	the minimum investment in CCDS pursuant to the Offer, being 500 CCDS (reflecting a minimum total consideration of approximately £50,000 per investor at the Issue Price).
<b>Minimum Transfer Amount</b>	a set minimum transfer amount for CCDS prevailing from time to time (being, as at the date of these Listing Particulars, 500 CCDS).
<b>Moody's</b>	Moody's Investors Service Limited.
<b>MREL</b>	the minimum requirement for own funds and eligible liabilities under BRRD and the Banking Act.
<b>NIM</b>	net interest margin
<b>Nominee</b>	Citivic Nominees Limited, in whose name the Global CCDS Certificate and Global Tier 2 Certificate will be registered, as nominee for Euroclear and Clearstream, Luxembourg (and such term shall include any successor or replacement nominee).
<b>Non-Executive Directors</b>	Julie Hopes Mark Preston Richard Sommers Colin Walklin James Turner Mark Nicholls Martin Ritchley
<b>NSFR</b>	net stable funding ratio.
<b>Offer</b>	the offer of the Securities to certain professional investors in the United Kingdom and elsewhere outside the United States and certain other jurisdictions, in reliance on Regulation S under the Securities Act or another exemption from, or in a transaction not subject to, the registration requirements of the Securities Act as described in " <i>Part VII: Distribution, Settlement and Transfers – 3. Selling Restrictions</i> ".
<b>Official List</b>	the Official List of the Luxembourg Stock Exchange.
<b>Open Banking</b>	the collective term used to describe the combined impact of new regulations such as the Competition and Markets Authority and PSD2, where certain financial institutions will provide registered third party organisations with transactional information where the consent of the customer or member is provided. The aim of Open Banking is to create

	more transparency and fairness in banking and financial services through greater competition and innovation.
<b>PDMR</b>	person discharging managerial responsibilities within the meaning of section 96B(1) of the FSMA.
<b>PFI</b>	private finance initiative.
<b>PIBS</b>	the Society's existing £75 million 6.15 per cent. permanent interest bearing shares.
<b>PPDS</b>	the Society's existing 3,650 profit participating deferred shares.
<b>PPI</b>	payment protection insurance.
<b>PRA</b>	the BoE acting as Prudential Regulation Authority through its Prudential Regulation Committee.
<b>Product Intervention Rules</b>	the Product Intervention (Contingent Convertible Instruments and Mutual Society Shares) Instrument 2015 and related rules under it (including COBS 22.2).
<b>Prospectus Directive</b>	Directive 2003/71/EC, as amended and includes any relevant implementing measure in each Relevant Member State.
<b>Protected Liabilities</b>	certain claims (including in respect of deposits and insurance policies) made against the Society by customers for whom the FSCS will pay compensation as the statutory fund of last resort if the Society is unable, or likely to be unable, to pay such claims.
<b>PSD2</b>	the revised Payment Services Directive (Directive (EU) 2015/2366 of the European Parliament and of the Council of 25 November 2015 on payment services in the internal market).
<b>RAO</b>	Financial Services and Markets Act 2000 (Regulated Activities) Order 2001
<b>Registrar</b>	Citibank N.A., London Branch.
<b>Regulation S</b>	Regulation S under the Securities Act.
<b>Relevant Member State</b>	each Member State of the European Economic Area that has implemented the Prospectus Directive.
<b>Relevant Regulators</b>	the PRA and/or the FCA as required in the circumstances.
<b>Resulting Society</b>	the amalgamated or transferee building society resulting from an amalgamation by the Society with another building society under section 93 of the Act or a transfer or all or substantially all of its engagements to another building society under section 94 of the Act.
<b>Results Announcement</b>	The announcement made by the Society on 10 April 2018 relating to the results of the LME.
<b>RMBS</b>	residential mortgage backed securities.

<b>RSL</b>	registered social landlord.
<b>Rules</b>	the Rules of the Society.
<b>RWAs</b>	risk weighted assets.
<b>S&amp;P</b>	Standard & Poor's Credit Market Services Europe Limited.
<b>SDLT</b>	stamp duty land tax.
<b>SDRT</b>	stamp duty reserve tax.
<b>Securities</b>	The CCDS and/or the Tier 2 Notes, as the context admits.
<b>Securities Act</b>	the US Securities Act of 1933, as amended.
<b>SMEs</b>	small and medium sized enterprises.
<b>SMR</b>	the Society's Standard Mortgage Rate.
<b>SRR</b>	the Special Resolution Regime under the Banking Act.
<b>Society</b>	West Bromwich Building Society, a building society incorporated in England and Wales under the Act and registered with the FCA on the Mutuels Public Register under number 651B.
<b>Stabilisation Options</b>	resolution tools available to Authorities under the SRR to resolve a bank or building society in circumstances in which the Authorities consider its failure has become highly likely and a threat is posed to the public interest.
<b>Successor Entity</b>	upon a transfer of the Society of the whole of its business in accordance with section 97 of the Act to a company, that company becomes the Successor Entity.
<b>Supervisory Authority</b>	the PRA or such successor or other authority having primary supervisory authority with respect to prudential matters concerning the Society.
<b>Surplus</b>	on a winding-up or dissolution of the Society, the surplus assets (if any) of the Society remaining following payment in full of the claims of all depositors and creditors (including subordinated creditors) of the Society (and, if applicable, after payment of the claim in respect of declared but unpaid Distributions).
<b>Tax Event</b>	as defined in Tier 2 Condition 18 in " <i>Part X: - Terms and Conditions of the Tier 2 Notes</i> ".
<b>TFS</b>	The BoE's Term Funding Scheme.
<b>Tier 2 Agency Agreement</b>	the agency agreement to be dated on or around 12 April 2018 between the Society and the Tier 2 Agent in relation to the Tier 2 Notes, as amended from time to time.
<b>Tier 2 Agent</b>	Citibank N.A., London Branch as registrar, transfer agent and principal

	paying agent in relation to the Tier 2 Notes.
<b>Tier 2 Conditions</b>	the terms and conditions of the Tier 2 Notes, as detailed in “ <i>Part X: - Terms and Conditions of the Tier 2 Notes</i> ”.
<b>Tier 2 Notes</b>	the tier 2 notes to be issued by the Society on or around 12 April 2018, as detailed in “ <i>Part X: - Terms and Conditions of the Tier 2 Notes</i> ”
<b>Transfer Agent</b>	the CCDS Agent or the Tier 2 Agent, as applicable.
<b>UK Corporate Governance Code</b>	the UK Corporate Governance Code dated April 2016 issued by the Financial Reporting Council, as amended from time to time.
<b>United Kingdom or UK</b>	the United Kingdom of Great Britain and Northern Ireland.
<b>United States or US</b>	the United States of America, its territories and possessions, any state of the United States of America and the District of Columbia.

