Pillar 3 Capital Disclosures

(under CRD IV)

for the year ended 31 March 2017

the West Brom

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Section 1 – **Overview**

Background

The European Parliament and Council approved new capital reforms which implemented Basel III into Europe from 1 January 2014. The new rules brought in by the EU regulations, the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD) applied through the Prudential Regulation Authority (PRA), are referred to collectively as CRD IV.

The objective of the reform package is to improve the banking sector's ability to absorb shocks arising from financial and/or economic stress, thus reducing the risk of spill-over from the financial sector into the wider economy.

CRD IV also sets out disclosure requirements relevant to banks and building societies under CRR Part Eight (Articles 431 to 455). These are known as Pillar 3 disclosures because they complement the minimum capital requirements in Pillar 1 and the supervisory review process in Pillar 2. The Pillar 3 disclosures are aimed at promoting market discipline by providing information on risk exposures and the management of those risks. Future reports will be expanded to include further disclosures in compliance with the timeline disclosed within the regulation.

For all exposures and risk areas the Standardised Approach is adopted.

The tables within this report show the Society regulatory measures on both a transitional basis per the PRA policy statement PS7/13 and an end point basis to reflect current expectations of where CRD IV will become binding.

The Financial Conduct Authority (FCA) and the PRA are responsible for the regulation of the Society. In this document the PRA and FCA are collectively described as 'the regulator'.

Basis and frequency of disclosure

This document sets out the 2017 Pillar 3 disclosures for the Society. These disclosures have been prepared solely to give information on the basis of calculating Basel III requirements and on the management of risks faced by the Society in accordance with the rules laid out in CRR Part Eight. The disclosures may differ from similar information in the 2017 Annual Report and Accounts prepared in accordance with International Financial Reporting Standards (IFRS); therefore the information in these disclosures may not be directly comparable with that information. All figures are as at 31 March 2017, the Society's year end, unless otherwise stated.

The CRR requires the Society to adopt a formal policy to comply with Pillar 3 disclosure requirements and the European Banking Authority (EBA) has issued guidelines on materiality, proprietary and confidential information and disclosure frequency. The Board has put in place such a policy and confirms that no disclosures have been omitted as either being proprietary or confidential.

Location and verification

These disclosures have been reviewed by the Risk Committee (RC) on behalf of the Group's Board and are published on the West Bromwich Building Society website (www.westbrom.co.uk). These disclosures have not been, and are not required to be, subject to independent external audit, and do not constitute any part of the Society's financial statements; however, some of the information within the disclosures also appears in the Group's audited Annual Report and Accounts.

Scope

For accounting purposes, the West Bromwich Building Society's consolidation Group comprises the Society itself and all of its subsidiary and quasi-subsidiary entities. For capital purposes the Group is ostensibly the same, except that it excludes two of its securitisation quasi-subsidiaries; Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc. These structured entities are not consolidated for capital purposes; a deduction is instead made against capital available for the residual risk relating to these entities which is retained by the Group. This treatment is adopted as the significant credit risk associated with the securitised exposures is considered to have been transferred to third parties (see Section 9 - Securitisation).

There is a requirement to calculate and maintain regulatory capital ratios on both a Group and "Society Solo consolidated basis". However, for West Bromwich Building Society, there are no material differences between the Group and Society Solo consolidation figures. Therefore, this document includes only the Group analysis.

The principal subsidiaries included for capital purposes are:

West Bromwich Mortgage Company Limited (includes quasi-subsidiary – Hawthorn Finance Limited);
West Bromwich Commercial Limited;
West Bromwich Homes Limited ;
Insignia Finance Limited;
Kenrick No. 1 Plc. (a quasi-subsidiary); and
Kenrick No. 2 Plc. (a quasi-subsidiary).

Full details of the principal subsidiary undertakings are included in Note 15 to the Annual Report and Accounts for the year ended 31 March 2017.

There are no material current or foreseen practical or legal impediments to the prompt transfer of capital resources or repayment of liabilities between the parent undertaking and its subsidiary undertakings.

Changes to disclosure requirements

In December 2016 the EBA published its final Guidelines on disclosure requirements under Part Eight, following an update of the Pillar 3 framework of the Basel Committee on Banking Supervision (BCBS) in January 2015. These Guidelines, while not changing the requirements of the regulatory disclosures defined in CRR Part Eight, provide further guidance and support to institutions to aid compliance with both the CRR and the updated BCBS Pillar 3 framework. The EBA Guidelines apply to Globally and Other Systemically Important Institutions ('G-SII' and 'O-SII' respectively) from 31 December 2017 with G-SIIs encouraged to comply with a sub-set of the Guidelines as soon as 31 December 2016. The Society is not a G-SII or O-SII but will give due and proportionate consideration to the Guidelines in future Pillar 3 disclosures.

Section 2 – **Risk management objectives and policies**

Overview

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

Categorisation

In order to identify the key risk categories most relevant to the Group, the Board considered an overall risk universe relating to firms in the financial services sector. This has been distilled into ten principal risk categories as shown below.

The main risks we manage are:

• Capital risk;	Section 4
• Credit risk;	Section 5
• Market risk, including interest rate risk and residential property holding risk;	Section 6
• Basis risk;	Section 6
• Operational risk;	Section 7
• Information risk;	Section 8
• Liquidity risk;	Section 8
• Pension liability risk;	Section 8
• Business risk; and	Section 8
• Retail conduct risk.	Section 8

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). Further information can be found on pages 23 to 27 of the Annual Report and Accounts for the year ended 31 March 2017.

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
First	Business Operations	Line Management	Line Management Oversight
Second	Policy, Controls, Measure, Monitor	Control Functions	Management and Board Committees
Third	Assurance	Internal Audit	Audit Committee

Table 1: Group's risk management framework

Governance structure

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

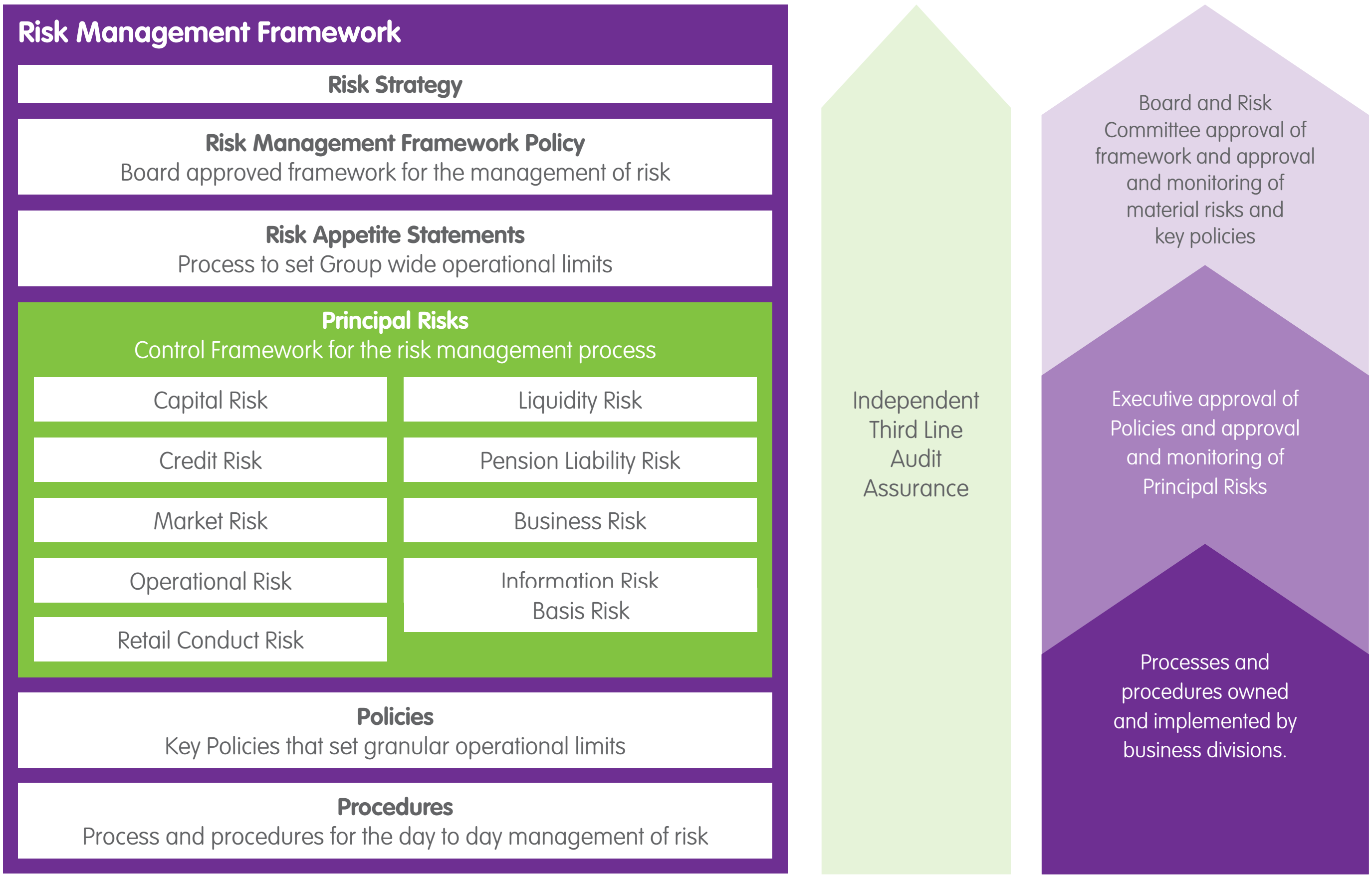
- **Risk Committee (RC)** – Comprising of all Non-Executive Directors except the Chairman, this Committee is responsible for the oversight and management of the principal and key strategic risks identified by the Board.
- **Executive Risk Committee (ERC)** – This Committee is chaired by the Chief Financial 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.
- **Group Capital Committee (GCC)** – This Committee is chaired by the Group Finance & Operations Director and is responsible for reviewing the Group's capital requirements.
- **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).
- **Audit Committee (AC)** – Comprising four Non-Executive Directors, the Audit Committee provides the Board with assurance regarding the integrity of the financial statements and the adequacy and effectiveness of the Society's risk management frameworks.

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

Section 2 – **Risk management objectives and policies** (continued)

Reporting on key risk measures

Reporting of key risk measures and escalation of issues across the Three Lines of Defence is critical in demonstrating that a risk management framework is designed and operating effectively. The risk management process consists of five key stages: Identify; Measure; Manage; Report; and Monitor. These stages are used to set clear standards for the consistent management of risk in each of the Principal Risk categories above. Reporting on the key risk measures occurs through the distribution of reports on the Principal Risks to Risk Committee and is shown in the chart below.



Risk strategy

The Group continues to focus on the needs of savers and borrowers and a key part of the risk culture is to put the interests of current and future members, as a whole, first. The Society has defined quantitative and qualitative risk parameters within which it is prepared to operate.

These parameters are designed to ensure the Group delivers acceptable returns, generates capital to support delivery of the business plan and support the exit of non-core business, balancing speed with economic cost. The Group's strategy and new lending activity focuses on prime residential owner occupied properties to good quality borrowers who can demonstrate their ability to meet their ongoing mortgage payments.

The Group's performance against risk measures and operational limits is reviewed regularly by the Executive Risk Committee and the Risk Committee.

The Society uses stress testing as a key management tool to gain a better understanding of the resilience of the Group to external and internal shocks. These tests form a key part of the Group's capital and liquidity assessment and are designed to confirm that the Group has sufficient capital and liquid resources, support effective forward-looking strategic plans and to ensure the Group stays within its risk appetite.

The Group undertakes scenario tests to understand and manage the impact of the occurrence of these events and for more severe scenarios has developed a Recovery Plan that details the options available to the Group and any obstacles to resolution.

Section 3 – **Capital resources**

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

	Notes	Transitional CRD IV rules 2017 £m	Full implementation of CRD IV 2017 £m	Transitional CRD IV rules 2016 £m	Full implementation of CRD IV 2016 £m
Common Equity Tier 1 capital					
General reserves		211.0	211.0	239.3	239.3
Revaluation reserve	1	3.5	3.5	3.4	3.4
Available for sale reserve		1.7	1.7	0.9	0.9
Cash flow hedging reserve		(0.7)	(0.7)	(0.3)	(0.3)
Profit participating deferred shares (PPDS)	2	173.0	173.0	179.5	179.5
Common Equity Tier 1 prior to regulatory adjustments		388.5	388.5	422.8	422.8
Regulatory adjustments:					
Defined benefit pension fund asset	3	-	-	(0.8)	(0.8)
Cash flow hedging reserve	4	0.7	0.7	0.3	0.3
Intangible assets and goodwill	5	(13.3)	(13.3)	(8.2)	(8.2)
Deferred tax asset relating to operating losses	6	(8.9)	(8.9)	(14.7)	(14.7)
Other adjustments	7	1.0	1.0	(2.4)	(2.4)
Common Equity Tier 1 (CET 1) capital		368.0	368.0	397.0	397.0
Additional Tier 1 capital					
Permanent interest bearing shares (PIBS)	8	75.0	75.0	74.9	74.9
Regulatory adjustments:					
Amortisation of PIBS under transitional rules		(37.5)	(75.0)	(30.0)	(74.9)
Total Tier 1 capital		405.5	368.0	441.9	397.0
Tier 2 capital					
Collective provision		22.1	22.1	18.1	18.1
Deduct: Contingency against collective provision add back	9	(2.5)	(2.5)	-	-
Total Tier 2 capital		19.6	19.6	18.1	18.1
Total capital		425.1	387.6	460.0	415.1

Table 2: Total available capital showing the Group position under both the transitional and full implementation basis of CRD IV

Tier 1 capital

Notes:

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 Common Equity Tier 1 (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 but rank pari-passu with 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. Further details about PPDS are provided in appendix 1 (capital instruments key features) and Note 27 to the Annual Report and Accounts and full terms and conditions of the Group's PPDS can be found on the Group's website: http://www.westbrom.co.uk/ppds-special-conditions.

Section 3 – **Capital resources** (continued)

Tier 1 capital (continued)

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 £0.5m (2016: £nil) and low quality mortgage backed security notes of £0.6m (2016: £2.4m) 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 £2.1m (2016: £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 rank pari-passu with PPDS. The holders of PIBS are not entitled to any share in any final surplus upon winding up or dissolution of the Society.

   With respect to future interest payments, as a condition of the PPDS, the Society has undertaken to pay an amount which, when annualised, represents the lower of: 6.15% of the outstanding principal amount of the PIBS and the dividend yield attributable to the PPDS with respect to the prior financial year ending 31 March whose payment is at the discretion of the Society. Further details about PIBS are provided in appendix 1 (capital instruments key features) and Note 26 to the Annual Report and Accounts and full terms and conditions of the Group's PIBS can be found on the Group's website, within the PIBS prospectus at pages 16 to 24 and the variation to the special conditions of issue of the PIBS:

   http://www.westbrom.co.uk/pibs-prospectus

   http://www.westbrom.co.uk/variations-to-pibs

   Under the transitional rules applicable to the current year, 50% (2016: 40%) 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.

Tier 2 capital

The Tier 2 capital comprises the Society's collective impairment provisions.

9. 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.

Reconciliation of regulatory capital

A reconciliation of total capital to regulatory capital is presented below:

At 31 March

	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
Total equity attributable to members per the Statement of Financial Position	**463.5**	**463.5**	497.7	497.7
Adjustments for items not eligible for inclusion in Common Equity Tier 1 capital:				
Retirement benefit asset	**-**	**-**	(0.8)	(0.8)
Cash flow hedging reserve	**0.7**	**0.7**	0.3	0.3
Intangible fixed assets and goodwill	**(13.3)**	**(13.3)**	(8.2)	(8.2)
Deferred tax asset relating to operating losses	**(8.9)**	**(8.9)**	(14.7)	(14.7)
Other adjustments	**1.0**	**1.0**	(2.4)	(2.4)
Total adjustments to Common Equity Tier 1 capital	**(20.5)**	**(20.5)**	(25.8)	(25.8)
Adjustments to Additional Tier 1 capital: Amortisation of PIBS under transitional rules	**(37.5)**	**(75.0)**	(30.0)	(74.9)
Adjustments to Tier 2 capital:				
Add back: Collective impairment allowance	**22.1**	**22.1**	18.1	18.1
Contingency against collective provision add back	**(2.5)**	**(2.5)**	-	-
Total adjustments to Tier 2 capital	**19.6**	**19.6**	18.1	18.1
Regulatory capital	**425.1**	**387.6**	460.0	415.1

Table 3: Reconciliation of accounting capital to regulatory capital

Section 3 – **Capital resources** (continued)

Regulatory capital flow statement

The table below shows the flow of regulatory capital and associated deductions in the year to 31 March 2017.

	£m
Common Equity Tier 1 capital at 1 April 2016	**397.0**
Loss for the period	**(25.8)**
Other comprehensive income recognised directly in general reserves	**(9.0)**
Increase in intangible fixed assets and goodwill	**(5.1)**
Reduction in the deferred tax asset relating to operating losses	**5.8**
Reduction of the defined benefit pension fund asset	**0.8**
Movement in revaluation reserve	**0.1**
Movement in available for sale reserve	**0.8**
Other movements	**3.4**
Common Equity Tier 1 capital at 31 March 2017	**368.0**
Additional Tier 1 capital at 1 April 2016	**44.9**
Unwind of discount on subscribed capital	**0.1**
Amortisation of PIBS under transitional rules	**(7.5)**
Additional Tier 1 capital at 31 March 2017	**37.5**
Tier 2 capital at 1 April 2016	**18.1**
Movement in collective impairment allowance	**4.0**
Contingency against collective provision add back	**(2.5)**
Tier 2 capital at 31 March 2017	**19.6**
Regulatory capital at 31 March 2017	**425.1**

Table 4: Regulatory capital flow statement under transitional CRD IV rules

Section 4 – **Capital adequacy**

Capital risk

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

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 (SREP) through which it sets the Society's capital requirements, expressed as Individual Capital Guidance (ICG) which covers the Pillar 2A 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 ICG, to cover losses that may arise under a severe stress scenario (Pillar 2B) after allowance for the CRD IV buffer (see below).

Section 4 – **Capital adequacy** (continued)

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 capital buffers from 1 January 2016, known as Pillar 2B. These comprise a Capital Conservation Buffer (CCoB); a Systemic Risk Buffer (SRB); and a macro-prudential Countercyclical Buffer (CCyB). 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.

The following diagram shows the constituent elements of the CRD IV capital requirement that could impact the Society, the phasing in of these requirements, and the quality of capital that can be used to meet the minimum requirement. Capital used to meet the firm-specific Pillar 1 and Pillar 2A and 2B capital requirements, which may include a firm-specific buffer, may not be used to meet the additional CRD IV supplementary buffers.

CRD IV risk adjusted capital requirements

PRA Buffer (Firm specific)	Applicable from 1 January 2016. Firm specific buffer assigned by the PRA if CCoB and CCyB buffers are considered to be insufficient.
Capital Conservation Buffer (CCoB)	Phased in from 2016 to 2019. Used to absorb losses in periods of economic and financial stress. 1.25% from 1 January 2017, increasing to 2.5% of RWAs by 1 January 2019.
Systemic Risk Buffer (SRB)	Full application from 1 January 2019 up to 3% of RWAs. Set at 0% of RWAs for institutions, including the Society, with total assets less than £175 billion.
Macro-prudential Countercyclical Buffer (CCyB)	The Financial Policy Committee (FPC) of the Bank of England uses core indicators, with other relevant economic and financial data, to set the CCyB (from 0% to 2.5% of RWAs). As at 31 March 2017 this was set at 0%.
Pillar 2A	Firm specific calculation for risks not fully captured under Pillar 1.
Pillar 1	Firm specific calculation based upon individual firms' risk weighted assets – a minimum of 8% of RWAs.

100% Common equity Tier 1

Minimum 56% Common equity Tier 1, up to 44% Additional Tier 1 (including a maximum of 25% Tier 2)

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 overleaf shows the Group's overall minimum capital requirement for credit, operational and market risk.

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) at 31 March 2017. Details of the Standardised Approach to the calculation of regulatory requirements are contained in CRD IV.

Section 4 – **Capital adequacy** (continued)

Minimum capital requirement – Pillar 1 (continued)

At 31 March

	2017 Average risk weights %	**2017 £m**	2016 Average risk weights %	2016 £m
Credit risk				
Residential mortgage loans (performing)	**35.4**	**119.4**	35.7	116.2
Commercial mortgage loans (performing)	**98.9**	**9.7**	97.7	15.2
Residential mortgage loans (past due)	**103.0**	**8.1**	102.1	9.4
Commercial mortgage loans (past due)	**146.1**	**42.6**	146.1	43.0
Liquidity (Treasury instruments and cash)	**11.9**	**7.7**	15.7	9.7
Other items	**100.0**	**14.1**	104.8	14.1
Total capital requirements – credit risk		**201.6**		207.6
Operational risk - Standardised Approach		**7.7**		7.6
Market and counterparty credit risk*		**3.8**		2.4
Total Pillar 1 capital requirement		**213.1**		217.6
Total capital available under transitional CRD IV rules		**425.1**		460.0
Excess of capital over minimum capital requirement under Pillar 1		**212.0**		242.4

Table 5: the Group's overall minimum Pillar 1 capital requirements under the Standardised Approach

* 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 brings more stringent requirements for the eligibility of capital instruments with a focus on Common Equity as the principal component of regulatory Tier 1 capital, and changes to the regulatory deductions from Common Equity. The regulations set a minimum of Tier 1 capital at 6% of Risk Weighted Assets (RWAs), of which Common Equity Tier 1 (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.

At 31 March

		Transitional CRD IV rules	**Full implementation of CRD IV rules**	Transitional CRD IV rules	Full implementation of CRD IV rules
	Minimum %	**2017 %**	**2017 %**	2016 %	2016 %
Common Equity Tier 1 ratio	**4.5**	**13.8**	**13.8**	14.6	14.6
Tier 1 ratio	**6.0**	**15.2**	**13.8**	16.2	14.6
Total capital ratio	**8.0**	**16.0**	**14.5**	16.9	15.3

Table 6: Group capital ratios

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 are not able to do this, and therefore will not be eligible as Tier 1 capital. These PIBS are 'grandfathered' and recognised as additional Tier 1 capital on an amortising basis (see Section 3).

Section 4 – **Capital adequacy** (continued)

Quality of capital (continued)

Profit Participating Deferred Shares (PPDS) eligibility challenge

A third party has alleged that the PPDS of the Society do not comply with one aspect of the CET1 Criteria. If this were to be correct, the Society would, over time, need to reduce the degree to which the PPDS count towards its CET1 capital, with the PPDS not included as CET1 included instead as Tier 2 capital.

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

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

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

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

The Directors consider that the Society will continue to remain adequately capitalised.

Leverage

CRD IV introduces 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%. For the Society this measure does not come into effect until 2018.

At 31 March

	Transitional CRD IV rules 2017 £m	**Full implementation of CRD IV rules 2017 £m**	Transitional CRD IV rules 2016 £m	Full implementation of CRD IV rules 2016 £m
Total Tier 1 capital (per table 2)	**405.5**	**368.0**	441.9	397.0
Total assets per the Statement of Financial Position	**5,830.8**	**5,830.8**	5,767.1	5,767.1
Mortgage pipeline and committed facilities	**72.1**	**72.1**	79.7	79.7
Common Equity adjustments relating to assets	**(20.5)**	**(20.5)**	(26.1)	(26.1)
Repurchase agreements and Potential Future Credit Exposure for swaps	**91.8**	**91.8**	38.5	38.5
Netted derivative adjustment	**(37.9)**	**(37.9)**	(70.0)	(70.0)
Adjusted assets	**5,936.3**	**5,936.3**	5,789.2	5,789.2
Leverage ratio (%)	**6.8**	**6.2**	7.6	6.9

Table 7: Group leverage ratio

At 31 March 2017 the leverage ratio of the Society was significantly above the 3% regulatory minimum. Under the transitional CRD IV provisions it was at 6.8 % (2016: 7.6%). Upon full implementation this will reduce to 6.2% (2016: 6.9%). There will be little change in the ratio during 2017/18, although asset quality will continue 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. The Society expects to continue to operate at a leverage ratio that is considerably in excess of the regulatory requirements including a buffer appropriate to the nature of its business model.

Section 4 – **Capital adequacy** (continued)

Risk Weighted Assets (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	**2,594.9**
Portfolio quality (increase)/decrease	(8.8)	1.3	(29.9)	(5.7)	**(43.1)**
Portfolio size increase/(decrease)	32.6	(74.7)	4.9	5.9	**(31.3)**
Risk Weighted Assets at 31 March 2017	1,594.3	654.4	95.7	176.1	**2,520.5**

Table 8: Risk Weighted Assets flow statement

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.

Section 5 – **Credit risk**

Credit risk overview

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.

The Society insures its residential mortgage book against losses using Mortgage Indemnity Guarantee (MIG) Insurance. MIG Insurance is taken on advances where the loan to value (LTV) exceeds 80% in line with its risk appetite. However, for prudence, no credit risk mitigation benefits have been taken from this purchase when assessing its Pillar 1 capital requirements.

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.

Analysis of treasury credit risk exposures

The following tables analyse the Group's regulatory credit risk exposures to Treasury counterparties. These include both on and off balance sheet exposures (after credit risk mitigation). They are therefore not directly comparable with the figures reported in Note 32 to the Annual Report and Accounts. The Group has no exposure in its liquidity portfolio to Cyprus, Greece, Ireland, Italy, Portugal or Spain, the emerging markets or to any mortgage market other than the UK.

At 31 March

	Notes	**2017 £m**	2016 £m	Average over year £m
Concentration by credit grading				
AAA to AA-		**701.4**	637.9	669.7
A+ to A-		**119.2**	148.2	133.7
Building societies		**-**	1.0	0.5
BBB+ to BBB-	1	**72.7**	17.4	45.0
BB+ to BB-	1	**1.9**	4.2	3.1
		895.2	808.7	852.0
Concentration by sector				
UK Government & Bank of England		**294.8**	215.4	255.1
Supranational financial institutions		**89.7**	53.5	71.6
Financial institutions		**257.4**	302.2	279.8
Asset backed securities		**253.3**	237.6	245.5
		895.2	808.7	852.0

Table 9: Analysis of the Group's regulatory credit risk exposures to Treasury counterparties

Notes:

1. These credit grading bands include investments in asset backed securities issued by Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc., quasi subsidiaries of the Society. Further details of these entities can be found in Section 9.

Section 5 – **Credit risk** (continued)

Analysis of treasury credit risk exposures (continued)

At 31 March

	2017 £m	2016 £m	Average over year £m
Concentration by region			
UK	**685.1**	580.4	632.7
Europe (excluding UK)	**71.0**	84.7	77.9
North America	**8.6**	34.1	21.4
Australasia	**10.2**	25.4	17.8
East Asia	**30.6**	30.6	30.6
Supranational financial institutions	**89.7**	53.5	71.6
	895.2	808.7	852.0

Table 9 (continued): Analysis of the Group's regulatory credit risk exposures to Treasury counterparties

Residual maturity breakdown of treasury exposures by asset class

The following table shows the residual maturity of exposures. With the exception of the asset backed securities, where it is assumed that the counterparty exercises their call option to redeem the notes, this is stated on a contractual rather than an expected basis, and does not take into account the cash flows payable or receivable over the life of the exposure. These encompass both on and off balance sheet exposures (after credit risk mitigation) and include the potential future exposure of derivatives.

Although not always directly comparable, an analysis of the maturity of the exposures for liquidity purposes can be found in Note 34 to the Annual Report and Accounts.

At 31 March 2017

	< 1 year £m	1 – 5 years £m	> 5 years £m	No specific maturity £m	**Total £m**
UK Government & Bank of England	287.6	-	-	7.2	**294.8**
Supranational financial institutions	24.2	65.5	-	-	**89.7**
Financial institutions	178.2	67.4	11.8	-	**257.4**
Asset backed securities	112.7	136.8	3.8	-	**253.3**
	602.7	269.7	15.6	7.2	**895.2**

At 31 March 2016

	< 1 year £m	1 – 5 years £m	> 5 years £m	No specific maturity £m	Total £m
UK Government & Bank of England	208.7	-	-	6.7	215.4
Supranational financial institutions	28.4	25.1	-	-	53.5
Financial institutions	282.0	20.2	-	-	302.2
Asset backed securities	32.8	200.6	4.2	-	237.6
	551.9	245.9	4.2	6.7	808.7

Table 10: Residual maturity analysis of liquidity exposures by asset class

Section 5 – **Credit risk** (continued)

Residual maturity breakdown of treasury exposures by asset class (continued)

The Group uses external credit ratings as part of its assessment of credit risk which are recognised by the Regulator as eligible External Credit Assessment Institutions (ECAI) for the purpose of calculating credit risk requirements under the Standardised Approach. Particular reference is made to the ratings published by Moody's and Fitch. There has been no change in the Groups use of ECAIs during the year.

The table below shows the exposure values associated with each credit quality step for on balance sheet Treasury exposures under the Standardised Approach.

At 31 March

	Notes	Risk Weight %	Fitch ratings	Moody's ratings	**2017 Exposure values £m**	2016 Exposure values £m
UK Government & Bank of England						
Credit quality step						
1	1	0	AA+	Aa1	**294.8**	215.4
Total					**294.8**	215.4
Supranational financial institutions						
Credit quality step						
1		0	AAA	Aaa	**89.7**	53.5
Total					**89.7**	53.5
Financial institutions						
Credit quality step						
1		20	AAA to AA-	Aaa to Aa3	**66.7**	135.0
2	2	50	A+ to A-	A1 to A3	**81.5**	111.8
3		50	BBB+ to BBB-	Baa1 to Baa3	**17.4**	16.9
Total					**165.6**	263.7
Asset backed securities						
Credit quality step						
1	3	20	AAA	Aaa	**249.5**	233.4
3	4	100	BBB+ to BBB-	Baa1 to Baa3	**1.9**	-
4	4	350	BB+ to BB-	Ba1 to Ba3	**1.9**	4.2
Total					**253.3**	237.6

Table 11: Analysis of the liquidity exposures into credit quality steps based on the ratings

Notes:

1. Includes cash in hand and Cash Ratio Deposit with the Bank of England.
2. Includes rated building societies.
3. The AAA asset backed securities all relate to prime loans secured on residential property located in the United Kingdom.
4. The asset backed securities with ratings below AAA, which relate to loans secured on commercial property located in the United Kingdom, were issued by Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc., quasi subsidiaries of the Society. Further details of these entities can be found in Section 9.

Capital required under Pillar 1 for liquidity was £7.7m (2016: £9.7m)

Section 5 – **Credit risk** (continued)

Treasury credit risk mitigation

The Group mitigates risk of loss arising from default by its derivative counterparties through legally enforceable Credit Support Annex (CSA) agreements. The CSAs require collateral to be posted against changes in the net mark to market value of derivative exposures with a particular counterparty. In the event of default, this collateral is transferred to the disadvantaged counterparty. These CSAs are taken into consideration when setting the internal credit risk limits for derivative counterparties and the Pillar 1 capital calculations. Market valuations used to determine the amount of cash collateral are performed daily or weekly depending upon the counterparty. No collateral is posted if the net change in market value for the period is less than a specified threshold amount.

'Wrong-way' risk may occur when an exposure to a counterparty is adversely correlated with the credit quality of the counterparty. The Society has no 'wrong-way' risk exposure and no appetite for such exposures. The Society mitigates 'wrong-way' risk by ensuring that exposures to derivatives are managed via CSA agreements, which are regularly re-margined and are collateralised with cash.

Concentration risk

The Group calculates credit risk for exposures secured by mortgages on residential properties and commercial real estate using the Standardised Approach.

The following table shows the Group's exposure to commercial loans by industry type.

At 31 March

	2017 £m	2016 £m
Residential	**18.7**	20.2
Healthcare & leisure	**134.2**	160.6
Industrial & warehouse	**8.7**	9.5
Office	**23.8**	29.5
Retail	**271.8**	306.7
Other	**18.4**	18.3
	475.6	544.8

Table 12: Analysis of the commercial loan portfolio by industry type

The following table shows the Group's exposure to commercial loans by region.

At 31 March

	2017 £m	2016 £m
East Anglia	**13.8**	13.8
East Midlands	**34.9**	36.0
Greater London	**53.7**	66.5
North	**34.2**	38.5
North West	**169.9**	192.1
Scotland	**12.0**	16.8
South East	**61.1**	72.2
South West	**13.3**	16.1
Wales	**1.6**	5.3
West Midlands	**40.7**	45.3
Yorkshire	**40.4**	42.2
	475.6	544.8

Table 13: Analysis of the commercial loan portfolio by geographic spread

Section 5 – **Credit risk** (continued)

Concentration risk (continued)

The following table shows the Group's exposure to residential loans by region.

At 31 March

	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	**207.6**	194.7
West Midlands	**705.7**	713.1
Yorkshire	**343.4**	301.1
	4,235.1	4,111.2

Table 14: Analysis of the residential loan portfolio by geographic spread

The following table shows the residual maturity of the Group's on-balance sheet exposures secured by mortgages on residential properties and commercial real estate after allowance for fair value and specific loss provisions.

At 31 March

	2017 £m	2016 £m
Up to 3 months	**254.6**	296.4
3-12 months	**69.6**	92.8
1-5 years	**306.3**	293.3
More than 5 years	**4,074.4**	3,968.7
	4,704.9	4,651.2

Table 15: Analysis of on-balance sheet loan exposures by residual maturity

Section 5 – **Credit risk** (continued)

Impairment of mortgage loans and advances

For a financial asset or a group of financial assets to be impaired, or impairment losses incurred, there needs to be objective evidence.

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

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

- deterioration in payment status;
- tenant failure;
- expected future increase in arrears due to change in loan status;
- breach of loan covenants; or
- any other information discovered during annual review suggesting that a loss is likely in the short to medium term.

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

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

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

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

Impairment losses on investment securities

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

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

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

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

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

Financial assets are written off when it is reasonably certain that receivables are irrecoverable.

Section 5 – **Credit risk** (continued)

Past due and impaired loans

'Past due loans' are defined as loans where the borrower's contracted payments have not been received by the due date.

The following tables provide an analysis of impaired and past due loans for residential and commercial lending. The figures in the tables include all Group companies but exclude the assets of the securitisation entities that are considered off balance sheet for regulatory purposes (see Section 9 – Securitisation). The Group does not consider the geographical spread of impaired exposures to be significant.

At 31 March

	2017 £m	2016 £m
Loans neither past due nor impaired	**4,156.1**	4,001.5
Past due but not impaired		
Past due 1 to 3 months	**21.5**	35.8
Impaired		
Not past due but impaired	**20.4**	21.8
Past due 1 to 3 months	**1.9**	0.8
Past due 3 to 6 months	**12.5**	16.2
Past due 6 to 12 months	**6.5**	16.0
Past due over 12 months	**3.4**	8.1
Possessions	**12.8**	11.0
	4,235.1	4,111.2

Table 16: Analysis of impaired and past due loans for residential lending

At 31 March

	2017 £m	2016 £m
Loans neither past due nor impaired	**293.3**	298.2
Not past due but impaired	**62.2**	122.5
Impaired		
Past due 1 to 3 months	**16.9**	5.0
Past due 3 to 6 months	**4.6**	6.5
Past due 6 to 12 months	**21.1**	11.1
Past due over 12 months	**77.5**	101.5
	475.6	544.8

Table 17: Analysis of impaired and past due loans for commercial lending

Section 5 – **Credit risk** (continued)

Impairment losses

The following table shows the movement during the year in impairment provisions. This analysis differs from that shown in Note 14 to the Annual Report and Accounts as it excludes amounts relating to Sandwell Commercial Finance No.1 Plc and Sandwell Commercial Finance No. 2 Plc where the credit risk associated with the securitised exposures is considered to have been transferred to third parties.

At 31 March 2017

	Residential lending		Commercial		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	**Total £m**
At 1 April 2016	11.8	9.0	30.6	9.1	42.4	18.1	**60.5**
Amounts written off	(1.0)	-	(13.2)	-	(14.2)	-	**(14.2)**
(Credit)/Charge for the year comprises:							
Provision for loan impairment	(0.7)	(0.8)	6.3	4.8	5.6	4.0	**9.6**
Adjustments to provisions resulting from recoveries	(2.0)	-	-	-	(2.0)	-	**(2.0)**
(Credit)/Charge for the year	(2.7)	(0.8)	6.3	4.8	3.6	4.0	**7.6**
At 31 March 2017	8.1	8.2	23.7	13.9	31.8	22.1	**53.9**

Table 18: Analysis of movement during the year ended 31 March 2017 in impairment provisions

At 31 March 2016

	Residential lending		Commercial		Total		
	Individual £m	Collective £m	Individual £m	Collective £m	Individual £m	Collective £m	Total £m
At 1 April 2015	15.8	8.7	31.7	7.5	47.5	16.2	63.7
Amounts written off	(3.8)	-	(7.5)	-	(11.3)	-	(11.3)
Charge/(Credit) for the year comprises:							
Provision for loan impairment	0.8	0.3	7.5	1.6	8.3	1.9	10.2
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
At 31 March 2016	11.8	9.0	30.6	9.1	42.4	18.1	60.5

Table 19: Analysis of movement during the year ended 31 March 2016 in impairment provisions

All impairments were against UK assets. All residential and commercial mortgage loans were secured against UK assets.

Capital required under Pillar 1 for mortgage loans (both performing and non-performing) was £179.8m (2016: £183.8m).

Forbearance strategies and renegotiated loans

A range of forbearance strategies is employed in order to work with borrowers to manage arrears and, wherever possible, avoid repossession. These are set out in the Society's relevant Group policies. The agreed strategy will reflect the customer's individual circumstances and will be used in line with industry guidance.

The principal forbearance measures provided by the Society on arrears cases are as follows:

- Arrangements, where monthly payments are maintained and the arrears are repaid over a period of time;
- Concessions, where it is agreed to accept the normal monthly payment with no contribution towards paying off the outstanding arrears, reduced payments or, in exceptional circumstances, no repayments for a short period;
- Capitalisation of arrears can be considered but only when the customer has made six consecutive monthly payments and arrears have not been capitalised within the prior five years;
- If the loan is on a repayment basis it may be put onto an interest-only scheme for a temporary period; and
- Mortgage term extensions to reduce the amount of the monthly payment may be considered as part of a longer-term solution.

Forbearance strategies and renegotiated loans (continued)

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

At 31 March

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

At 31 March

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

Table 20: Residential mortgage balances with renegotiated terms at the year end date

Some of these 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.

Section 5 – **Credit risk** (continued)

Forbearance strategies and renegotiated loans (continued)

The analysis below sets out the commercial mortgage balances with evidence of forbearance and renegotiated terms at the year end date.

At 31 March

	Arrangements 2017 £m	**Capitalisation 2017 £m**	**Term extensions 2017 £m**	**Total 2017 £m**
Loans neither past due or impaired	**6.6**	**-**	**44.4**	**51.0**
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**
Total	**22.6**	**11.2**	**55.3**	**89.1**

At 31 March

	Arrangements 2016 £m	Capitalisation 2016 £m	Term extensions 2016 £m	Total 2016 £m
Loans neither past due or impaired	0.2	-	66.1	66.3
Not past due but impaired	3.7	11.3	15.8	30.8
Impaired				
Past due over 12 months	19.3	-	-	19.3
Total	23.2	11.3	81.9	116.4

Table 21: Commercial mortgage balances with evidence of forbearance and renegotiated terms at the year end date

Section 5 – **Credit risk** (continued)

Counterparty credit risk

Counterparty credit risk (CCR) is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows. CCR differs from credit risk in that exposure at default is calculated. It arises where a counterparty default may lead to losses of an uncertain nature and this uncertainty is factored into the valuation of the Group's credit exposure using the mark to market method plus an add-on for potential future exposure.

Such transactions relate to contracts for financial derivative instruments, securities financing transactions and long settlement transactions. The Group uses derivative instruments to hedge its exposure to market risk, for example, interest rate risk. Risk is mitigated by offsetting the amounts due to the same counterparties ("netting benefits") and by cash deposited by certain of the counterparties ("collateral held").

The following table shows the exposures to CCR for derivative contracts:

At 31 March

	2017 £m	2016 £m
Interest rate contracts	**2.9**	2.1
Other contracts	**3.4**	6.7
Gross positive fair value of contracts	**6.3**	8.8
Cash collateral and netting benefits	**(6.3)**	(8.8)
Net derivatives credit exposure	**-**	-

Table 22: CCR for derivative contracts

Capital required under Pillar 1 for Market risk, including CVA and exposures to Secured Financing Transactions totals £3.8m (2016: £2.4m). The exposure to derivatives is calculated using the CCR Mark to Market method.

The net derivatives credit exposure represents the credit exposure to derivative transactions after taking account of legally enforceable collateral arrangements.

The Society has entered into International Swaps and Derivatives Association (ISDA) master netting agreements for all of its derivatives, whereby outstanding transactions with the same counterparty can be settled net following a default or other predetermined event. Credit Support Annexes (CSAs) are executed in conjunction with these ISDA master agreements which typically provide for the exchange of collateral on a weekly basis to mitigate net mark to market credit exposure.

Whilst exchange traded derivatives have been cleared through central counterparties (CCPs) for many years, recent regulatory initiatives designed to reduce systemic risk in the banking system are directing increasing volumes of Over the Counter (OTC) derivatives to be cleared through CCPs. The Society now transacts all new qualifying swaps through Central Counterparties.

The net exposure value of derivatives at 31 March 2017 was £9.7m (2016: £9.3m) which includes an amount for potential future exposure.

Section 6 – **Market risk**

Market risk

Market risk refers to the possible changes in the value of, or income arising from, the Society's assets and liabilities as a result of changes in interest/exchange rates, property prices or equities. Market risk exposures are managed through the Treasury department which is responsible for managing exposure to all aspects of market risk within parameters set by the Board. ALCo reviews the Treasury Policy, recommending changes to the Board as appropriate, and ensures that regular reports on all aspects of market risk are assessed and reported to the Board.

Interest rate risk

The key market risk is interest rate risk, which arises as a result of differences in the timing of interest rate re-pricing of assets and liabilities. To mitigate this, Treasury uses natural balance sheet hedging (e.g. matching 2 year fixed rate mortgages with 2 year fixed rate saving bonds) and derivative instruments. The use of derivatives is only permitted in accordance with the provisions of the Building Societies Act 1986, which focus on their use to reduce risk. The maximum level of interest rate risk is governed by the Board approved Treasury Policy in line with the Board's risk appetite.

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

Basis risk

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

Interest rate risk summary

The levels of Group pre-tax interest rate risk exposures, to a +2% parallel shift, through the reporting period were as follows:

	As at 31 March 2017 £m	Average 2017 £m	High 2017 £m	Low 2017 £m
Market value	**(2.1)**	(0.9)	(2.1)	0.2
Net interest income	**(0.5)**	(0.6)	(1.2)	(0.3)

Table 23: Group Interest Rate risk exposures

No capital is required under Pillar 1 for this element of market risk.

Derivative activity

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

Section 6 – **Market risk** (continued)

Other market risk

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

The Society has invested in property through its subsidiary West Bromwich Homes Limited and offers residential property for rent.

This non-core business exposes the Society to movements in house prices. The Board's strategy is to exit from this business when market conditions are opportune.

Although it is recognised that controls cannot eliminate the risk of holding the properties, the controls which were in place both when acquiring the property and in the ongoing management of the property help to reduce the risk (no additional properties are being acquired). The key controls include:

At acquisition

- Properties were required to have appeal for both owner occupation and buy to let; and
- Properties located in areas with consistent demand for both owner occupation and buy to let properties.

Ongoing management

- Use of a specialist property management agency to ensure the properties remain in a marketable condition whilst optimising rental yields; and
- Property values monitored on a monthly basis with a formal revaluation at least annually.

Section 7 – **Operational risk**

Operational risk overview

The Group has applied a commonly used definition of 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.

The Society has adopted The Standardised Approach (TSA) for the calculation of its Operational Risk Capital Requirement (ORCR), which establishes the Society's minimum Pillar 1 capital requirement for operational risk. This is calculated from the average of the last three years income, with the income allocated to defined business lines being subject to a prescribed multiplier. As a mutual lender, the Society's ORCR is primarily derived from retail banking activities.

In order to ensure that the Society's ORCR is suitable for extreme events, management assesses its suitability through the development of a series of stress test scenarios used to estimate the impacts of extreme but plausible low frequency, high impact loss events. These are considered in isolation and in combination to develop a range of potential impacts. The outputs of the scenarios are then used to inform management whether further capital requirements are required for operational risk, in addition to the ORCR.

Operational risk framework

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.

Operational risk management and mitigation

Operational Risk is further classified into sub-categories (level 2 risks), all of which are overseen by a Divisional Director. Each level 2 risk has a documented strategy, updated annually, which sets out the approach to managing the risk. Each strategy is based on the following principles: there is a Board approved risk definition; there is a Three Lines of Defence Model, with clearly articulated responsibilities for the management of each risk; there are appropriate policies, processes, systems and controls throughout the Society; and finally, a defined governance structure. Second line control testing is conducted in accordance with the annual controls testing plan agreed by the Risk Committee.

Key operational risks and their mitigants are detailed below:

Risk	Brief description	Operational risk management and mitigation
Business Continuity and Disaster Recovery Risk	The risk of failure to adequately assess, document, test and invoke business continuity procedures to safeguard Group assets and personnel, and to adequately maintain or re-commence all essential business operations following a business continuity event.	Each business area has a Business Continuity Plan, reviewed every 6 months. There is a Crisis Management Plan with a defined Crisis Management Team. Testing activities are led by the 2nd line according to the plan agreed by Risk Committee. Examples include bi-annual Work Area Recovery tests, call cascades and desktop exercises with the Crisis Management Team.
Customer Operations Risk	The risk of financial and non-financial impacts resulting from inadequate or failures in customer facing/support processes.	Customer Operations Risks are most concentrated within the Operations function and the branch network, where activity is focussed on customer transactions, occurring by any means, primarily by post and email (Operations), telephone (Operations and branches) or in person (branches). The management and control of these risks is integral to the provision of service. 1st line control activities are carried out locally (or by a specialist area outside the team).
Product risk	The risk of financial and non-financial impacts resulting from the inadequate design and launch of new products and services.	Product Consideration Group is the 1st line Committee in the Product Governance Framework, which ensures that risks are mitigated and the Society delivers its obligation for the fair treatment of customers at the following stages: design and governance; identifying target markets; marketing and promotion; sales and advice processes; after-sales information and service; and complaints handling. Other controls include Product Design Risk Assessments and on-going monitoring of 3rd parties.
Financial Reporting Risk	Failure to interpret and comply with financial reporting and taxation requirements, including the misrepresentation of financial statements.	There is dedicated resource within the Finance department, which has systems and controls in place for regulatory reporting. This is supported by 2nd line controls testing and utilisation of external advisors where required.
Model Risk	Risk of errors in the design, implementation or operation of models.	Controls surround the design, development, approval, implementation and review of computer based tools (typically spreadsheets) that are used to support business decision making.
Technology Risk	The risk of financial and non-financial impacts resulting from failures in the development, delivery, maintenance and continuity of effective IT systems.	There is dedicated IT resource to implement the development, delivery, maintenance and continuity of effective IT systems. Oversight is provided by the Operational & Conduct Risk Group (OCRG) and ultimately the Risk Committee.

Section 7 – **Operational risk** (continued)

Risk	Brief description	Operational risk management and mitigation
People Risk	The risk associated with the ability to recruit, develop, motivate and retain the required number and quality of people. People risk includes failure to comply with employment related requirements and inappropriate or unauthorised employee activity.	The management of People related risks is the responsibility of all managers, whilst the Human Resources department maintains oversight. On a day-to-day level, Human Resources provides advice and support to the business in relation to Recruitment and Selection, Employee Relations, Reward, Learning and Development approaches and Payroll and Administration in adherence to employment legislation and Society policies.
Legal & Regulatory Risk	The risk of regulatory censure, fines or legal action as a result of incorrect or inappropriate business conduct, e.g. failure to comply with legislative / regulatory requirements or Codes of Conduct.	Legal and Regulatory risk is managed by the Group Secretary under a separate reporting line to the Chief Executive. The Group has a small internal Legal team and selectively uses external firms where specific legal support is required.
Physical Assets, Safety and Security Risk	The risk that appropriate premises and other physical assets are not available to support business operational needs or do not conform to all relevant regulations, including Health and Safety requirements. It includes theft of/ damage to the Society's assets and threats or actual harm to the Society's employees.	Central to managing this risk is the Health & Safety Policy, Information Security Policy and the Physical Security Policy. A dedicated Corporate Facilities department, managed by the Divisional Director HR, provides specialist support to 1st line areas. As well as the standard risk governance arrangements, additional oversight is provided by the Health & Safety Committee.
Supplier & Outsourcing Risk	The risk of adverse impacts arising from services with outsourced partners or third-party suppliers. It includes inappropriate supplier selection and management processes and failure on the part of the supplier to deliver the agreed services and/or comply with relevant laws, codes and ethical behaviours.	Business areas play a key first line role by setting out procedures and processes to ensure compliance with both the risk management strategy and the Procurement Policy. Controls are in place throughout all stages of procurement, including ongoing contract and supplier management.
Financial Crime Risk	Risk of financial and non-financial impacts arising from internal and external fraud, or from a failure to comply with financial crime legislation.	The Group Secretary retains overall responsibility and oversight of Financial Crime Risk as part of his Money Laundering Reporting Officer responsibilities. The Head of Operational & Conduct Risk is responsible for the day to day running of the Financial Crime Team. The Group pays close attention to the source, likelihood and impact of Financial Crime.
Change Risk	The risk of financial and non-financial impacts resulting from the inadequate design, management or implementation of change.	Controls exist to ensure change is delivered in a controlled manner, whether it be Business As Usual change (such as a process change without systems development); small process or organisational change where operational and customer impact is low; or project change, where the risk and complexity demands a formal approach to change. For the latter, specific controls include an agreed project methodology and governance arrangements.

Operational risk oversight and governance

Oversight and governance arrangements for the setting and management of a robust operational risk management policy and framework are the responsibility of the Board and supported by the OCRG.

Capital required under Pillar 1 for operational risk was £7.7m (2016: £7.6m).

Section 8 – **Other risks**

This section sets out the other risks faced by the business above and beyond the Pillar 1 risks set out in sections 4 to 7.

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.

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

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

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

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

The Society has also set up an Information Risk Group. The Group 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) across the Society. Its purpose is to support and drive the information risk governance agenda and provide the Society with the assurance that effective information governance best practice mechanisms are in place within the Society.

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.

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

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

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

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

Section 8 – **Other risks** (continued)

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. The Scheme is also exposed to possible changes in pension legislation.

The Group has funding obligations for a defined benefit scheme, the Staff Retirement Scheme ("the Scheme"), which is closed to new members and no longer accruing service benefits.

To mitigate these risks, management, together with the Trustees of the Scheme, regularly reviews reports prepared by the Scheme's independent actuaries to assess these risks and take appropriate actions which may, for example, include adjusting the investment strategy or contribution levels to address any funding deficit.

Business risk

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

This is the risk to the Society arising from changes in its business, including the risk that it may not be able to carry out its business plan and its desired strategy or both. This may be due to changes in the competitive environment or events which damage the operating economies of the Group (e.g. competitor activity, changes in regulation or taxation).

The Group regularly models the impact of a range of scenarios on the business plans, with a view to identifying mitigating actions.

Retail conduct risk

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

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

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

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

- A clearly articulated and Board approved Conduct Risk Appetite Statement;
- An embedded and compliant Conduct Risk Management Framework;
- A Three Lines of Defence model with clearly articulated responsibilities for the management of conduct risk;
- Appropriate business processes, a centralised risk management system used by business areas to manage their risks and controls to support the effective management of conduct risk across the Society; and
- Committee oversight within an appropriate governance structure, in particular the 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.

Section 9 – **Securitisation**

Securitisation risk is the residual credit risk arising from retaining an interest in the Group's securitisation companies through the provision of subordinated debt and/or start up expense loans and liquidity facilities where applicable.

Originated securitisations

Securitisation is the process by which a ring fenced group of assets, usually loans, are aggregated into a pool, and sold to structured entities. The pool of mortgage loans is used to back the issuance of new securities, allowing the credit rating of the securities to be separated from the credit rating of the originating entity. The Group has established securitisation structures as part of its funding activities, using residential and commercial mortgage loans as the underlying asset pools.

The equity of the structured entities created for these securitisations is not owned by the Group. However, to comply with the Building Societies Act 1986 (International Accounting Standards and Other Accounting Amendments) Order 2004 and IFRS 10, the structured entities are included as subsidiaries in the consolidated financial statements. This is despite the fact that some structured entities may be structured to cap group exposures to losses at levels which mean that consolidation is not considered to be appropriate for capital purposes.

The Group has experience of issuing securitisations under various programmes, and has built up a depth of knowledge, processes and management information to deal effectively with these funding vehicles. Securitisation has historically been used to increase the diversification of funding sources, manage maturity mismatch risk, and assist overall credit risk management.

Treatment of securitisations for capital purposes

There are two distinct capital treatments for the securitisations that the Group has originated. The capital treatment is dependent upon whether or not significant credit risk associated with the securitised exposures is considered to have been transferred to third parties. The mortgage originator usually retains an element of risk by holding a tranche of subordinated loans. Where the risk is limited to a relatively small tranche of subordinated loans it is usually possible to demonstrate that a significant risk transfer has taken place. Where this is the case, the structured entity is not consolidated for capital purposes and no risk weighted exposures are included in the capital calculation for the assets that have been securitised, instead the subordinated loans net of any deductions arising from consolidated losses are deducted from Tier 1 capital. Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc are not consolidated for capital purposes.

Alternatively, where the structures do not achieve significant risk transfer, the underlying mortgage pools and other assets of the securitisations remain within the Group and are consolidated for capital purposes. This means the assets are risk weighted along with the Group's own assets using the Standardised Approach as reported in Section 4 – Capital Adequacy. Hawthorn Finance Limited, Kenrick No 1 Plc and Kenrick No 2 Plc are treated in this manner.

Non-consolidated structured entities for regulatory capital purposes

The Group, through its subsidiary company, West Bromwich Commercial Limited (WBCL), provides subordinated loans (including funding for start-up costs) to Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc.

The notes in these securitisations are serviceable firstly from cash flows generated by the mortgage assets and thereafter from the proceeds of the subordinated loans. The Group receives the excess spread on the transactions as deferred consideration, after the structured entities have met their liabilities. The Group does not provide any liquidity facilities to the structured entities. WBCL provides administration and cash management services to the structured entities, for which it receives a fee. The subordinated start-up loan balances have been written down to £nil (2016: £nil) by the application of cumulative losses on the securitised loans within Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc.

The structured entities were originally set up as follows:

Sandwell Commercial Finance No. 1 Plc
In May 2004, WBCL sold £250m of commercial mortgage assets, at book value, to Sandwell Commercial Finance No. 1 Plc. Sandwell Commercial Finance No. 1 Plc issued notes to finance the purchase of the commercial mortgage assets.

Sandwell Commercial Finance No. 2 Plc
In September 2005, WBCL sold £350m of commercial mortgage assets, at book value, to Sandwell Commercial Finance No. 2 Plc. Sandwell Commercial Finance No. 2 Plc issued notes to finance the purchase of the commercial mortgage assets.

The balances of gross assets subject to securitisation, notes in issue and underlying balances impaired and past due are included in the table below. Gross assets include the gross value of the underlying mortgage loans together with cash, cash equivalents and other assets.

Securitisation Company	Type	Date of Securitisation	Gross assets securitised 2017 £m	External notes in issue 2017 £m	Underlying assets past due and impaired 2017 £m	Gross assets securitised 2016 £m	Total notes in issue 2016 £m	Underlying assets past due and impaired 2016 £m
Sandwell Commercial No. 1 Plc	Commercial mortgage securitisation	19 May 2004	18.0	20.2	4.4	28.5	27.5	4.5
Sandwell Commercial No. 2 Plc	Commercial mortgage securitisation	23 September 2005	55.7	46.3	6.0	66.0	55.4	2.5
Total			73.7	66.5	10.4	94.5	82.9	7.0

Table 24: Assets subject to off balance sheet securitisation, notes in issue and impaired and past due assets.

The gross assets securitised in Table 24 are subject to impairment provisions of £1.8m (2016: £4.2m)

Section 9 – **Securitisation** (continued)

Consolidated structured entities for regulatory capital purposes

The structured entities, which are fully consolidated for capital purposes, were originally set up as follows:

Hawthorn Finance Limited
In July 2008, West Bromwich Mortgage Company sold £1,000m of residential buy to let mortgage assets, at book value, to Hawthorn Asset Co Limited, which in turn, borrowed funds from Hawthorn Finance Limited to fund the purchase of the mortgage assets.

Kenrick No. 1 Plc
In April 2012, an Originator Trust was created over a £343m portfolio of prime residential mortgages, at book value. Kenrick No. 1 Plc acquired a 99% share in the Originator Trust and issued notes to finance the purchase. The Society retained a 1% share in the Originator Trust. On 11 April 2017, the Society's triggered its call option and the loans were bought back by the Society.

Kenrick No. 2 Plc
In May 2013, an Originator Trust was created over a £426.3m portfolio of prime residential mortgages, at book value. Kenrick No. 2 Plc acquired a 99% share in the Originator Trust and issued notes to finance the purchase. The Society retained a 1% share in the Originator Trust.

Loan notes created under a retained securitisation may be used to raise funding. However, the loan assets within the securitisations do not change and we continue to manage the interest rate risk of the underlying mortgage assets.

To manage interest rate risk, the structured entities enter into derivative transactions with external derivative counterparties, paying a rate of interest based on the securitised mortgages and receiving a rate inherent in the debt issuances. Cash flows arising from these derivatives are accounted for on an accruals basis. The derivatives relating to the securitisations are treated as explained in the accounting policy, which can be found in the Annual Report and Accounts for the year ended 31 March 2017.

The structured entities are subject to legal covenants which need to be fulfilled in the event of a downgrade of the contracted liquidity provider. The cash flows resulting from these legal covenants are in respect of amounts held in the transaction bank accounts and the Guaranteed Investment Contract accounts, representing the net cash position arising from the management of the SPEs at any point in time. Funds may need to be either deposited with another institution with the requisite rating or a guarantee obtained from a suitable guarantor (in the event of the liquidity or derivative provider losing its short term rating unless the rating agencies confirm that the current ratings of the notes will not be affected). The cash flows affected solely relate to cash held within the SPVs and no further flows from the Society would be required.

The balances of assets subject to securitisation, notes in issue and underlying balances past due and impaired are included in table 25. Underlying assets past due and impaired are part of the totals reported within Table 16 for residential and Table 17 for commercial balances.

Securitisation Company and date of securitisation	**Type**	**Gross assets securitised 2017 £m**	**Total notes in issue 2017 £m**	**Retained notes in issue 2017 £m**	**Underlying assets past due and impaired 2017 £m**	Gross assets securitised 2016 £m	Total notes in issue 2016 £m	Retained notes in issue 2016 £m	Underlying assets past due and impaired 2016 £m
Hawthorn Finance Limited 22 July 2008	Residential mortgage securitisation	**742.0**	**712.7**	**712.7**	**2.5**	822.3	789.9	789.9	2.9
Kenrick No. 1 Plc 30 April 2012	Residential mortgage securitisation	**129.7**	**110.6**	**52.6**	**0.6**	164.2	145.1	52.6	0.4
Kenrick No. 2 Plc 28 May 2013	Residential mortgage securitisation	**219.4**	**186.5**	**-**	**0.9**	274.7	244.0	40.6	2.9
Total		**1,091.1**	**1,009.8**	**765.3**	**4.0**	1,261.2	1,179.0	883.1	6.2

Table 25: Assets subject to on balance sheet securitisation and notes in issue.

The issued securitisation notes are rated by Moody's and Fitch.

Purchased securitisation positions

The Group also invests in mortgage backed securities. The treatment of the Group's investment in mortgage backed securities is covered under Section 5 – Credit Risk.

Purchases and retention of residential mortgage backed securities are undertaken within a clearly defined credit risk policy. All residential mortgage backed securities holdings are monitored on a daily basis and if the credit rating deteriorates below AAA level the position is reviewed. The liquidity of residential mortgage backed securities assets held, either through sale or repo, is regularly tested by Treasury and reported accordingly. The Society holds no re-securitisations.

The Group has invested in commercial mortgage backed securities issued by Sandwell Commercial Finance No. 1 Plc and Sandwell Commercial Finance No. 2 Plc. As at 31 March 2017 these notes had a book value of £4.5m (2016: £6.6m) and of these, £3.8m (2016: £4.2m) was risk weighted and £0.6m (2016: £2.4m) was deducted from available Tier 1 capital. The minimum capital requirement for the risk weighted element was £0.7m (2016: £1.2m).

The valuation process of our investments in securitisation exposures primarily focuses on quotations from third parties and observed trade levels. This process did not change in 2016/17.

Section 10 – **Asset encumbrance**

Templates A and C are as prescribed in EBA Guideline EBA/GL/2014/03 on disclosure of encumbered and unencumbered assets. The values disclosed are the median values for the quarters ending in the year to 31 March 2017.

The carrying amount of encumbered assets in Template A row 010 column 010 is in respect of on balance sheet assets only and therefore excludes off balance sheet Funding for Lending Scheme (FLS) treasury bills. The amount shown in Template C row 010 column 030 includes both encumbered on and off balance sheet assets and therefore includes off balance sheet FLS treasury bills.

Template A – Assets

		Carrying amount of encumbered assets £m	**Fair value of encumbered assets £m**	**Carrying amount of unencumbered assets £m**	**Fair value of unencumbered assets £m**
2017		010	040	060	090
010	**Assets of the reporting institution**	1,181.8		4,597.8	
030	Equity instruments	-	-	-	-
040	Debt securities	5.0	5.0	377.3	377.9
120	Other assets*	-		215.1	

		Carrying amount of encumbered assets £m	Fair value of encumbered assets £m	Carrying amount of unencumbered assets £m	Fair value of unencumbered assets £m
2016		010	040	060	090
010	Assets of the reporting institution	1,218.5		4,463.4	
030	Equity instruments	-	-	-	-
040	Debt securities	31.8	32.5	343.3	347.2
120	Other assets*	-		241.3	

Table 26: Assets

* Other assets include derivative financial assets; property plant and equipment; intangible assets; prepayments; deferred tax assets; pension benefit surplus and investment properties. These assets would not be available for encumbrance in the normal course of business.

Template B – Collateral received

The EBA Guideline allows competent authorities to waive the requirement to disclose Template B – Collateral received, and in Supervisory Statement SS11/14 (CRD IV; compliance with the European Banking Authority's Guidelines on the disclosure of encumbered and unencumbered assets) the PRA waived the Template B requirements subject to a firm meeting certain criteria. The Society meets the criteria and therefore Template B is not disclosed.

Template C – Encumbered assets/collateral received and associated liabilities

2017		**Matching liabilities, contingent liabilities or securities lent £m**	**Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m**
		010	030
010	**Carrying amount of selected financial liabilities**	301.9	497.4

2016		Matching liabilities, contingent liabilities or securities lent £m	Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m
		010	030
010	Carrying amount of selected financial liabilities	245.3	382.2

Table 27: Encumbered assets/collateral received and associated liabilities.

Section 10 – **Asset encumbrance** (continued)

Template D – Information on importance of encumbrance

The most material sources of encumbrance for the Society are secured funding via the Society's securitisation programmes which are supported by pledging mortgage assets. Further detail on these activities is set out in note 13 to the 2017 Annual Report and Accounts. The Society also pledges debt securities as collateral in sale and repurchase transactions - see note 38 to the 2017 Annual Report and Accounts.

An additional source of encumbrance is the collateralisation of derivatives liabilities. The Society also treats some loans and advances to credit institutions and some debt securities as encumbered even though there are no associated liabilities. An example of this would be liquid assets held within the Group's securitisation programmes as these are not available for use in the Group's day-to-day operations.

In common with many other financial institutions, the Society began to make increasing use of secured funding from the start of the financial crisis.

The over collateralisation in Template C predominantly represents over-collateralisation in respect of the externally issued securitisation programmes, of treasury bills drawn down under the FLS scheme and encumbered assets with no corresponding liabilities.

A general description of terms and conditions of the collateralisation agreements entered into for securing liabilities are available in the 2017 Annual Report and Accounts as follows; for sale and repurchase transactions of debt securities in note 38.

Section 11 – **Remuneration and other corporate governance**

Governance arrangements

Disclosure requirements relating to governance arrangements under CRR Part Eight Article 435 are included in Section 2 of this report but are also supplemented by the disclosures included in the Directors' Report on Corporate Governance on pages 33 to 36 and Annual Business Statement on pages 111 to113 within the 2017 Annual Report and Accounts. The 2017 Annual Report and Accounts are published on the Society's website (www.westbrom.co.uk).

Remuneration

The responsibilities and decision-making process for determining remuneration policy and membership of the management body, the link between pay and performance and the design and structure of remuneration, including the performance related pay plans, have been disclosed in the 2017 Annual Report and Accounts on pages 40 to 46.

These disclosures meet the requirements of CRD IV and the PRA's Remuneration Code ('the Code'), for the Society's Directors and are not repeated here. The 2017 Annual Report and Accounts also refer to Code staff but do not include the details of remuneration required under CRD IV. This information is therefore set out below.

Code staff

Under the Code, the Society is required to identify those staff that are considered to have a material impact on the Society's risk profile. This includes all Executive Directors, Divisional Directors and Non-Executive Directors. These individuals are defined as 'Code Staff'.

The table below sets out the aggregate quantitative remuneration for Code Staff in relation to their services for the West Brom for the year ended 31 March 2017. The number of beneficiaries includes Code Staff with full and part year service. The remuneration figures below do not include severance pay which is shown separately in table 29.

Year to 31 March 2017

	Number of beneficiaries	Fixed remuneration* £000	Variable remuneration (non-deferred) £000	Deferred variable pay from previous years £000	Total remuneration £000	*Outstanding deferred remuneration £000*
Non-Executive Director	**7**	**492**	**-**	**-**	**492**	**-**
Executive Director	**3**	**888**	**161**	**105**	**1,154**	**216**
Other Code staff	**9**	**1,234**	**234**	**121**	**1,589**	**300**
Total	**19**	**2,614**	**395**	**226**	**3,235**	**516**

Year to 31 March 2016

	Number of beneficiaries	Fixed remuneration* £000	Variable remuneration (non-deferred) £000	Deferred variable pay from previous years £000	Total remuneration £000	*Outstanding deferred remuneration £000*
Non-Executive Director	6	437	-	-	437	-
Executive Director	2	858	161	94	1,113	213
Other Code staff	9	1,085	202	95	1,382	226
Total	17	2,380	363	189	2,932	439

Table 28: Aggregate quantitative remuneration of Code Staff.

* Includes fees, basic salary, pension and other benefits.

Section 11 – **Remuneration and other corporate governance** (continued)

Code staff (continued)

Remuneration for Code Staff

Component	Purpose	Operation	Performance Metrics
Basic Pay	Reflects level of responsibility.	Reviewed annually (or more frequently if required) linked to performance or market benchmarking.	Influencing factors include: • Role and experience; • Personal performance; • Benchmarking comparisons; and • Salary increases awarded across the Society.
Performance-Related Pay	Linked to the delivery of Society and personal objectives. Used to reward within the context of achieving the Society's goals and objectives.	Maximum annual opportunity for Executive Directors and Divisional Directors is 50% of basic salary. 40% of the Performance-Related Pay earned (maximum 20% of basic salary) is deferred over a three year period. Non-Executive Directors do not receive variable remuneration.	Based on a number of measures, including: • Financial; • Customer; • People; • Risk; and • Enhanced operational capabilities. Reviewed by the Committee annually to ensure that the measures are appropriate.
Pension or Pension Allowance	A part of fixed remuneration intended to attract and retain individuals of sufficient calibre.	Executive Directors and Divisional Directors are invited to join the Society's stakeholder pension plan or, as an alternative, be provided with a cash allowance. Non-Executive Directors do not receive a pension or pension allowance.	Not applicable.
Benefits	To provide market competitive remuneration.	Benefits are provided in line with market practice for Executive Directors and Divisional Directors, which include a fully expensed car, private medical care and life assurance. Other benefits may be provided in individual circumstances.	Not applicable.

A proportion of variable remuneration earned by Code Staff in the current financial year is deferred to subsequent years. Performance–related pay deferred to future years is subject to review by the Remuneration Committee and approved by the Board at the appropriate time before any payment is made.

There were no sign-on payments or variable remuneration in the form of share or share-like instruments and no individual received remuneration in excess of EUR 1 million.

Severance payments

Year to 31 March

	Number of beneficiaries	Severance pay £000	Highest individual award £000
2017	-	-	-
2016	1	115	115

Table 29: Aggregate severance pay of Code Staff

The severance payments reflect the contractual amounts payable.

Section 12 – **Adequacy of risk management controls**

The Board confirms that the Risk Management Report contained in the Annual Report and Accounts for the year ended 31 March 2017 and the Pillar 3 disclosures above are a fair description of the principal risks and uncertainties that the Group faces. The Board aims to manage effectively all the risks that arise from its activities and believes that the risk management arrangements and controls put in place are adequate with regards to the Group's profile and strategy. The principal external threats facing the Society are outlined in the 2017 Annual Report and Accounts on pages 26 and 27.

By order of the Board

Section 13 – **Contacts**

Should you have any queries please contact:

Manjit Hayre	Chief Financial Risk Officer
Tom Lynch	Divisional Director, Treasury and Finance
Jacqui Randle	Divisional Director, Human Resources
Neil Noakes	Group Secretary

West Bromwich Building Society. Head Office: 2 Providence Place, West Bromwich B70 8AF. Register Number 104877

Section 14 – **Glossary**

Basel II framework
The Basel Committee on Banking Supervision's statement of best practice that defines the methods by which firms should calculate their regulatory capital requirements to retain enough capital to protect the financial system against unexpected losses. The framework is structured around Pillars 1, 2 & 3, became law in the EU Capital Requirements Directive, and was implemented in the UK by the FSA (now PRA/FCA) Handbook.

Basel III
In December 2010, the Basel Committee on Banking Supervision issued the Basel III rules text, which presents the details of the strengthened global regulatory standards on bank capital adequacy and liquidity. The requirements, embedded using CRD IV, became effective from 1 January 2014.

Capital Requirements Regulation and Capital Requirements Directive IV (CRD IV)
CRD IV is the legislative package made up of the Capital Requirements Regulation and the Capital Requirements Directive to implement the Basel III agreement.

Counterparty Credit Risk (CCR) Mark to Market method
One of the methods allowed under the Standardised Approach for determining exposure values for financial derivative instruments.

Counterparty credit risk
Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows.

Commercial lending
Loans secured on commercial assets. Commercial assets can include office buildings, industrial property, hotels, medical centres, shopping centres, farm land, buy to let and housing association properties.

Common Equity Tier 1 capital (CET1)
CET1 capital comprises internally generated capital from general reserves and other reserves less intangible assets, goodwill and other regulatory adjustments.

Common Equity Tier 1 capital ratio
Common Equity Tier 1 capital as a percentage of Risk Weighted Assets.

CQS (Credit Quality Steps)
A credit quality assessment scale as set out in CRD IV.

CRD IV Buffers
These comprise a Capital Conservation Buffer (CCoB); a Systemic Risk Buffer (SRB); and a macro-prudential Countercyclical Buffer (CCyB).

Credit risk
The potential to incur losses from the failure of a borrower or counterparty to meet its obligation to pay interest or repay capital on an outstanding loan.

Credit risk mitigation
Techniques to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, the assignment of receivables or the use of credit derivatives, guarantees, credit insurance, set off or netting.

ECAI
External Credit Assessment Institution. An ECAI (e.g. Moody's, Standard and Poor's and Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.

FCA
Financial Conduct Authority. On 1 April 2013 the FCA replaced the FSA as the financial services industry regulator for conduct related matters.

Forbearance
Forbearance takes place when a concession, which can be temporary or permanent, is made on the contractual terms of a loan in response to the borrower's financial difficulties.

FSA
Financial Services Authority. The financial services industry regulator in the UK up to 31 March 2013 when its responsibilities were transferred to the Prudential Regulation Authority (PRA) and the Financial Conduct Authority (FCA).

Guarantee
An agreement by a third party to cover the potential loss to a credit institution should a specified counterparty default on their obligations.

ICAA
Internal Capital Adequacy Assessment - the document produced by the Society as a result of the ICAAP.

ICAAP
Internal Capital Adequacy Assessment Process. The process the Group follows to determine capital requirements under Basel III Pillar 2.

ICG
Individual Capital Guidance. The minimum amount of capital the Group should hold as set by the regulator under Basel III following a SREP exercise and a review of the Society ICAAP.

Individually/collectively assessed
At each Statement of Financial Position date the Group assesses whether or not there is objective evidence that individual financial assets are impaired. If no objective evidence of impairment exists for an individually assessed financial asset, it is included in a group of financial assets with similar credit risk characteristics and collectively assessed for impairment. A collective provision is made against a group of financial assets where there is evidence that credit losses have been incurred, but not individually identified, at the reporting date.

Interest rate risk
Interest rate risk is the exposure of a firm's financial condition to adverse movements in interest rates.

International Swaps and Derivatives Association (ISDA) master agreement
A standardised contract developed by ISDA and used to enter into bilateral derivatives transactions.

Leverage ratio
Tier 1 capital as a percentage of total exposures which include on and off balance sheet assets after netting derivatives.

LIBOR
London Inter-Bank Offered Rate.

Liquidity risk
The risk that the Group does not have sufficient financial resources to meet its obligations as they fall due, or will have to do so at an excessive cost. This risk arises from mismatches in the timing of cash inflows and outflows.

LTV
Loan-to-Value. The ratio of current exposure value as a proportion of the value of the asset held as security (usually residential property) expressed as a percentage.

Market risk
The risk that movements in market risk factors, including foreign exchange rates, interest rates, credit spreads and customer-driven factors will reduce income or portfolio values.

Maturity
The remaining time in years that a borrower is permitted to take to fully discharge their contractual obligation (principal, interest and fees) under the terms of a loan agreement.

Section 14 – **Glossary** (continued)

Minimum capital requirement
The minimum amount of regulatory capital that a financial institution must hold to meet the Basel III Pillar 1 requirements for credit and operational risk.

NED
Non-Executive Director.

Netting
The ability to reduce credit risk exposures by offsetting the value of any deposits against loans to the same counterparty.

Operational risk
Operational risk is 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.

PFE
The Potential Future Exposure is an estimate of the exposure relating to the future cash flows of derivatives. It is based upon the remaining duration and the type of the derivative.

PIBS
Permanent Interest Bearing Shares. Unsecured, deferred shares that, under transitional rules, are a form of Additional Tier 1 capital. PIBS rank behind the claims of depositors and creditors of the Society and equally with the Society's PPDS.

Pillar 1
The part of the Basel III Framework which sets out the regulatory minimum capital requirements for credit and operational risk.

Pillar 2
The part of the Basel III Framework which sets out the processes by which financial institutions review their overall capital adequacy. Supervisors then evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the assessments. This includes all risks (including Pillar 1 risks). The ICG is an outcome from Pillar 2.

PPDS
Profit Participating Deferred Shares are unsecured deferred shares that are a form of Common Equity Tier 1 capital. PPDS rank behind depositors and creditors of the Society and equally with the Society's PIBS.

PRA
Prudential Regulation Authority. From 1 April 2013, the PRA replaced the FSA as the financial services industry regulator in the UK for prudential matters.

PRA Buffer
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, but avoiding duplication with the CRD IV buffers.

Provisions
Amounts set aside to cover losses associated with credit risks.

RWA
Risk Weighted Assets. The value of an on or off-balance sheet exposure adjusted under Pillar 1 rules to reflect the degree of risk it presents.

Securitisation
A transaction or scheme where assets are sold to a Structured Entity in return for immediate cash payment. That entity raises the immediate cash payment by issuing debt securities in the form of tradeable notes or commercial paper to wholesale investors who receive an income from the underlying assets. Some risk is retained on the balance sheet while the remaining risk is transferred to investors.

SREP
Supervisory Review and Evaluation Process. The Regulator's assessment of a firm's own capital adequacy assessment (ICAAP) under Basel III Pillar 2.

Stress testing
Various techniques that are used to gauge the potential vulnerability to exceptional but plausible events.

Supranational Financial Institution
A Supranational Financial Institution is formed and capitalised by two or more central governments to promote economic development for specified member countries. Supranational Financial Institutions finance their activities by issuing bond debt and are usually considered part of the high quality, sub-sovereign debt market. Some well-known examples of Supranational Financial Institutions are the World Bank, European Bank for Reconstruction and Development, European Investment Bank, Asian Development Bank and Inter-American Development Bank.

The Standardised Approach (credit risk)
The Standardised Approach to credit risk, calculated by applying varying RWA percentages to credit exposures, depending on the underlying risk.

The Standardised Approach (operational risk)
The Standardised Approach to operational risk, calculated using three year historical net income multiplied by a factor of 12-18%, depending on the underlying business being considered.

Wrong-way risk
An adverse correlation between the counterparty's probability of default and the mark to market value of the underlying transaction.

Appendix 1 – **EBA capital instruments key features disclosure template**

The table below shows the capital instruments currently issued by the group.

		PPDS	PIBS
1.	Issuer	West Bromwich Building Society	West Bromwich Building Society
2.	ISIN	n/a	GB00B0CX2M20
3.	Gov. law (sub)	English	English
4.	Trans. CRR rules	CET1	Additional Tier 1
5.	Post-transitional CRR rules	CET1	Ineligible
6.	Eligible at Group (G), Individual Consolidated (IC) or Society (S)	G, IC, S	G, IC, S
7.	Instrument type (types to be specified)	Profit participating deferred shares	Permanent interest bearing shares
8.	Regulatory capital value (£)	£173.0m	£75.0m
9.	Nominal amount of instrument	£184.1m	£75.0m
9a.	Issue px	100.0	99.8
9b.	Redemption px	n/a	100.0
10.	Accounting classification	Shareholders equity	Shareholders equity
11.	Original date of issuance	10/08/2009	29/07/2005
12.	Perpetual or dated	Perpetual	Dated
13.	Original maturity date	No maturity	No maturity
14.	Issuer call	No	Yes 05/04/2021
15.	Optional call date, contingent call dates and redemption	n/a	21/04/2021
16.	Subsequent call dates, if applicable	n/a	Half yearly
17.	Fixed or floating dividend/coupon	Floating	Floating with cap
18.	Coupon rate and any related index	25% of Society's net loss or profit	Lower of 6.15% and rate paid to PPDS holders
19.	Existence of a dividend stopper	No[1]	Yes[2]
20a/b.	Fully discretionary, partially discretionary or mandatory	Fully discretionary	Fully discretionary
21.	Existence of step up or other incentive	No	Yes
22.	Non-cumulative or cumulative	Non-cumulative	Non-cumulative
23.	Convertible or non-convertible	Non-convertible	Non-convertible
30.	Write-down features	PPDS reduced in value by 25% of any net loss of the Society.	No
31.	If write-down, write-down triggers	Net loss	n/a
32.	If write-down, full or partial	Partial	n/a
33.	If write-down, permanent or temporary	Temporary	n/a
34.	If temporary write-down, description of write-up mechanism	Write-back dependent on Society making net profits. No dividends paid until capital shortfall paid off	n/a
35.	Instrument type immediately senior	Tier 2	Tier 2
36.	Non-compliant transitioned features	No	Yes
37.	If yes, specify non-compliant features	n/a	Step-up
	Full terms and conditions of the instruments can be found at:	http://www.westbrom.co.uk/ppds-special-conditions	http://www.westbrom.co.uk/pibs-prospectus http://www.westbrom.co.uk/variations-to-pibs

Specific rows that are not relevant to the Society's capital instruments have been omitted.

Notes:

1. The PPDS contain a term which requires reduction or cancellation of interest on our 6.15% PIBS in certain circumstances. Based on legal opinion obtained by the Society this is not a dividend stopper, as that term is generally understood, as the term applies exclusively to the 6.15% PIBS and not to any other instruments.
2. The dividend stopper in the PIBS prohibits payment of interest or dividends on any other class of deferred shares, other than the PPDS, only for a period of 5 months from the Board's decision to reduce or cancel interest on the PIBS.

See note 8 on page 7 for further details.

Appendix 2 – **EBA Countercyclical Capital Buffers disclosure templates**

The countercyclical buffer is an additional requirement introduced by CRD IV, calculated by applying a weighted average of country countercyclical buffer rates based on the geographical distribution of relevant exposures to the overall capital requirements of the Society. The following templates disclose information relevant for the calculation of the countercyclical buffer as at 31 March 2017 in accordance with Regulation (EU) 2015/1555 on a consolidated basis.

Template A: Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer

In accordance with Regulation (EU) 1152/2014, as foreign credit exposures represent less than 2% of the Society's aggregate risk weighted exposures, all exposures have been allocated to the UK. Exposures are as defined in Regulation (EU) 2015/1555 and in particular exclude exposures to sovereigns.

Row		General Credit Exposure value for SA	Securitisation Exposure value for SA	Own Funds requirements: Of which: General credit exposures	Own Funds requirements: Of which: Securitisation exposures	Own Funds requirements: Total	Own fund requirement weights	Countercyclical capital buffer rate
		10	50	70	90	100	110	120
	Breakdown by country	£m	£m	£m	£m	£m	Weighting	%
10	UK	5,110.4	115.5	195.8	2.5	198.3	1.0	0.0
20	Total	5,110.4	115.5	195.8	2.5	198.3	1.0	0.0

Table 30: Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer.

Amount of institution-specific countercyclical capital buffer

Row		Column
		10
10	Total risk exposure amount	£2,558m
20	Institution specific countercyclical buffer rate	0%
30	Institution specific countercyclical buffer requirement	£0m

Table 31: Amount of institution-specific countercyclical capital buffer.

Appendix 3 – **EBA Own Funds disclosure template**

	Common Equity Tier 1 (CET1) Capital: instruments and reserves	Transitional 2017 £m	Full Implementation 2017 £m	Transitional 2016 £m	Full Implementation 2016 £m
1	Capital instruments and the related share premium accounts	**173.0**	**173.0**	179.5	179.5
2	Retained earnings	**211.0**	**211.0**	239.3	239.3
3	Accumulated other comprehensive income (and other reserves) *	**6.6**	**6.6**	4.0	4.0
5	Common Equity Tier 1 (CET1) capital before regulatory adjustments	**390.6**	**390.6**	422.8	422.8
Common Equity Tier 1 (CET1) capital: regulatory adjustments					
7	Additional value adjustments (negative amount)	**(0.5)**	**(0.5)**	-	-
8	Intangible assets (net of related deferred tax liability) (negative amount)	**(13.3)**	**(13.3)**	(8.2)	(8.2)
10	Deferred tax assets that rely on future profitability excluding those arising from temporary differences (net of related tax liability where the conditions in Article 38 (3) are met) (negative amount)	**(8.9)**	**(8.9)**	(14.7)	(14.7)
11	Fair value reserves related to gains or losses on cash flow hedges	**0.7**	**0.7**	0.3	0.3
15	Defined-benefit pension fund assets (negative amount)	**-**	**-**	(0.8)	(0.8)
20a	Exposure amount of the following items which qualify for a RW of 1250%, where the institution opts for the deduction alternative	**(0.6)**	**(0.6)**	(2.4)	(2.4)
20c	of which: securitisation positions (negative amount)	**(0.6)**	**(0.6)**	(2.4)	(2.4)
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	**(22.6)**	**(22.6)**	(25.8)	(25.8)
29	Common Equity Tier 1 (CET1) capital	**368.0**	**368.0**	397.0	397.0
Additional Tier 1 (AT1) capital: instruments					
32	Capital instruments classified as equity under applicable accounting standards	**37.5**	**-**	44.9	-
36,44	Additional Tier 1 (AT1) capital	**37.5**	**-**	44.9	-
45	Total Tier 1 Capital	**405.5**	**368.0**	441.9	397.0
Tier 2 Capital **Tier 2 (T2) capital: instruments and provisions**					
50	Credit risk adjustments	**19.6**	**19.6**	18.1	18.1
51,58	Total Tier 2 Capital	**19.6**	**19.6**	18.1	18.1
59	Total Capital	**425.1**	**387.6**	460.0	415.1
60	Total risk weighted assets	**2,664.1**	**2,664.1**	2,720.4	2,720.4
Capital ratios and buffers					
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	**13.8%**	**13.8%**	14.6%	14.6%
62	Tier 1 (as a percentage of total risk exposure amount)	**15.2%**	**13.8%**	16.2%	14.6%
63	Total capital (as a percentage of total risk exposure amount)	**16.0%**	**14.5%**	16.9%	15.3%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**8.0%**	**6.5%**	8.9%	7.3%

Table 32: EBA Own Funds disclosure templates.

* In the template above, other comprehensive income includes an adjustment to add back the loss within the risk remote securitisations that was deducted from accounting reserves £2.1m (2016: £nil).

In line with EBA guidelines, specific rows that are not considered to be relevant to the Society's activities or for which the information provided would not be material have been omitted.

Appendix 4 – **EBA Leverage Ratio disclosure templates**

Reference Date	**31 March 2017 (31 March 2016 for comparatives)**
Entity Name	**West Bromwich Building Society**
Level of application	**Consolidated**

Template A:Table LRSum: Summary reconciliation of accounting assets and leverage ratio exposures

		2017 Transitional £m	**2017 Full Implementation £m**	2016 Transitional £m	2016 Full Implementation £m
1	Total assets as per published financial statements	**5,830.8**	**5,830.8**	5,767.1	5,767.1
4	Adjustments for derivative financial instruments	**(28.2)**	**(28.2)**	(60.7)	(60.7)
5	Adjustments for securities financing transactions "SFTs"	**82.1**	**82.1**	29.2	29.2
6	Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	**72.1**	**72.1**	79.7	79.7
7	Other adjustments	**(20.5)**	**(20.5)**	(26.1)	(26.1)
8	**Total leverage ratio exposure**	**5,936.3**	**5,936.3**	**5,789.2**	**5,789.2**

Template B:Table LRCom: Leverage ratio common disclosure

		2017 Transitional £m	**2017 Full Implementation £m**	2016 Transitional £m	2016 Full Implementation £m
	On balance sheet exposures (excluding derivatives and SFTs)				
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**5,824.5**	**5,824.5**	5,758.2	5,758.2
2	(Asset amounts deducted in determining Tier 1 capital)	**(20.5)**	**(20.5)**	(26.1)	(26.1)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)**	**5,804.0**	**5,804.0**	5,732.1	5,732.1
	Derivative exposures				
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	**9.7**	**9.7**	9.3	9.3
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	**(31.6)**	**(31.6)**	(61.1)	(61.1)
11	**Total derivative exposures (sum of lines 4 to 10)**	**(21.9)**	**(21.9)**	(51.8)	(51.8)
	Securities financing transaction exposures				
12	Gross SFT assets (with no recognition of netting), after adjusting for sales accounting transactions	**82.1**	**82.1**	29.2	29.2
16	**Total securities financing transaction exposures (sum of lines 12 to 15a)**	**82.1**	**82.1**	29.2	29.2
	Other off-balance sheet exposures				
17	Off-balance sheet exposures at gross notional amount	**144.2**	**144.2**	159.4	159.4
18	(Adjustments for conversion to credit equivalent amounts)	**(72.1)**	**(72.1)**	(79.7)	(79.7)
19	**Other off-balance sheet exposures (sum of lines 17 to 18)**	**72.1**	**72.1**	79.7	79.7
	Capital and total exposures				
20	**Tier 1 capital**	**405.5**	**368.0**	441.9	397.0
21	**Total leverage ratio exposures (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)**	**5,936.3**	**5,936.3**	5,789.2	5,789.2
22	**Leverage ratio (%)**	**6.8%**	**6.2%**	7.6%	6.9%
EU-23	Choice on transitional arrangements for the definition of the capital measure	**Transitional**	**Full Implementation**	Transitional	Full Implementation

Table 33: EBA Leverage Ratio disclosure templates.

Appendix 4 – **EBA Leverage Ratio disclosure templates** (continued)

Template C: Table LRSpl: Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)

		2017 Transitional £m	2017 Full Implementation £m	2016 Transitional £m	2016 Full Implementation £m
EU-1	**Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:**	**5,792.9**	**5,792.9**	5,697.1	5,697.1
EU-3	**Banking book exposures, of which:**	**5,792.9**	**5,792.9**	5,697.1	5,697.1
EU-4	Covered bonds	**137.8**	**137.8**	124.0	124.0
EU-5	Exposures treated as sovereigns	**386.4**	**386.4**	269.8	269.8
EU-7	Institutions	**187.5**	**187.5**	263.4	263.4
EU-8	Secured by mortgages of immovable properties	**4,262.2**	**4,262.2**	4,166.5	4,166.5
EU-9	Retail exposures	**42.4**	**42.4**	67.8	67.8
EU-10	Corporate	**7.8**	**7.8**	32.2	32.2
EU-11	Exposures in default	**463.8**	**463.8**	483.6	483.6
EU-12	Other exposures (e.g. equity, securitisations, and other non-credit obligation assets)	**305.0**	**305.0**	289.8	289.8

Table 33 (continued): EBA Leverage Ratio disclosure templates.

Template D: Table LRQA– Qualitative information on risk of excessive leverage and factors impacting the leverage ratio

1 Description of the processes used to manage the risk of excessive leverage

The Group's leverage ratio is a key financial indicator monitored by the Board each month. The leverage ratio is projected for the next five years as part of the Corporate Planning process. The Corporate Plan is subject to stress tests to ensure the Group is able to operate safely and with sufficient capital and leverage during a severe downturn in the general economy and idiosyncratic Society only stress events. It is recognised that such forward planning is essential to the successful management of the Group's leverage and capital ratios. The Board is satisfied that the risk appetite, controls and planning framework will prevent the group from taking excessive leverage within its balance sheet.

2 Description of the factors that had an impact on the leverage Ratio during the period to which the disclosed leverage Ratio refers

The Group's leverage ratio has reduced by 0.8% to 6.8% (2016: 7.6%). The reduction is due to the Group loss for the year. Further information relating to the loss can be found within the Annual Report and Accounts for the year ended 31 March 2017.

In line with EBA guidelines, specific rows that are not considered to be relevant to the Society's activities or for which the information provided would not be material have been omitted.

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