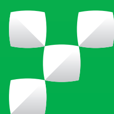
PILLAR 3 DISCLOSURES 2018



YORKSHIRE BUILDING SOCIETY

Contents

Capital Position at a Glance 2

1 Overview 3

1.1 Background 3

1.2 Basis, policy and frequency of disclosures 3

1.3 Scope 3

1.4 Capital management principles and risk appetite 4

1.5 Location and verification 5

1.6 Regulatory Developments 5

1.7 Recent Developments 5

2 Capital Resources 6

2.1 Total Available Capital 6

2.2 Tier 1 Capital 6

2.3 Tier 2 Capital 7

2.4 Reconciliation of Regulatory Capital to Balance Sheet Capital 8

2.5 Capital Flow Statement 9

3 Capital Requirements 10

3.1 Overview 10

3.2 Pillar 1 10

3.3 Capital Adequacy 15

3.4 RWA Flow Statement 15

3.5 Pillar 2A 16

3.6 Total Capital Requirement 16

3.7 Regulatory Capital Buffers 16

3.8 Leverage Ratio 16

3.9 Minimum Requirement for Eligible Liabilities (MREL) 17

3.10 IFRS 9 18

3.11 Stress Testing Results 19

3.12 Impact of CRD IV 19

3.13 Internal Capital Adequacy Assessment Process (ICAAP) 21

4 Risk Management 22

5 Credit Risk 23

5.1 Credit Risk Overview 23

5.2 Credit Risk Exposures 23

5.3 Securitisation Positions 32

5.4 Impairment Provisions 35

5.5 Credit Risk Concentrations 36

5.6 Credit Risk Mitigation 37

5.7 Counterparty Credit Risk for Derivative Contracts 38

6 Operational Risk 39

6.1 Operational Risk Overview 39

6.2 Enterprise Risk Management Framework (ERMF) and Governance 39

6.3 Operational Risk Oversight and Reporting 40

7 Other Risks 42

7.1 Interest Rate Risk 42

7.2 Pension Risk 42

7.3 Concentration Risk 42

7.4 Business Risk 42

7.5 Other Risks 42

8 Liquidity Management 43

8.1 Principles 43

8.2 Internal Liquidity Adequacy Assessment Process (ILAAP) 44

8.3 Liquidity Coverage Ratio (LCR) 44

9 Remuneration 47

10 Appendix 48

10.1 Appendix 1 - Asset Encumbrance 48

10.2 Appendix 2 - Own Funds Disclosure Template 50

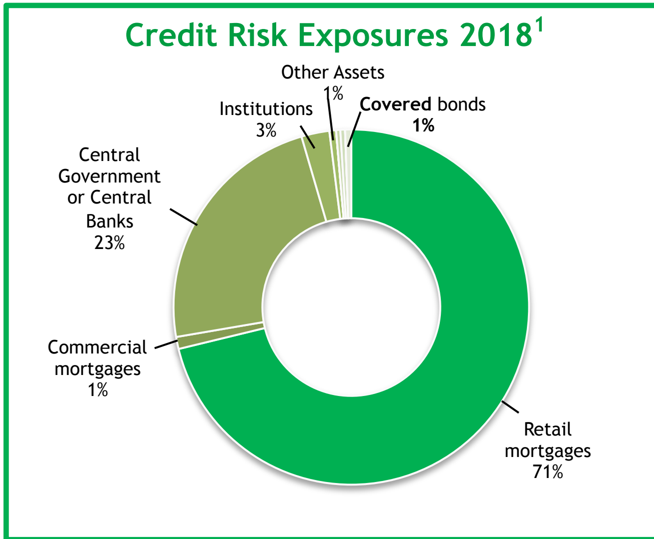
10.3 Appendix 3 - Capital Instruments Main Features Template 54

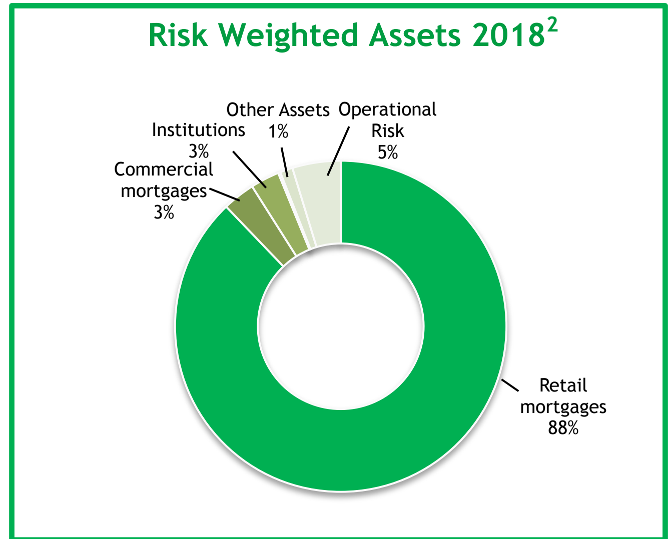
10.4 Appendix 4 - Leverage Disclosure Template 56

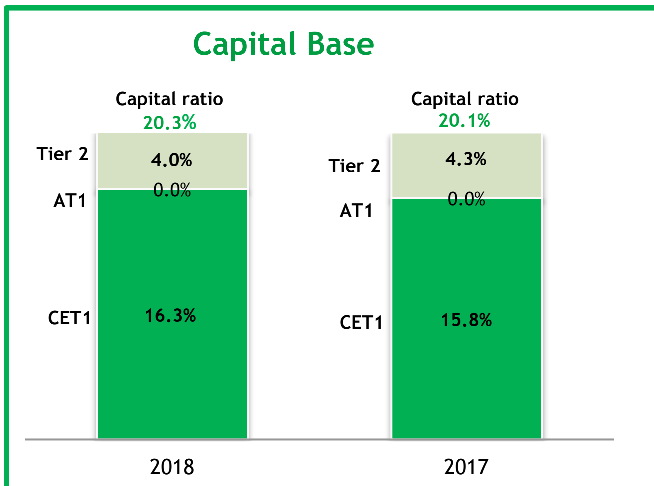
10.5 Appendix 5 - Countercyclical Capital Buffer 58

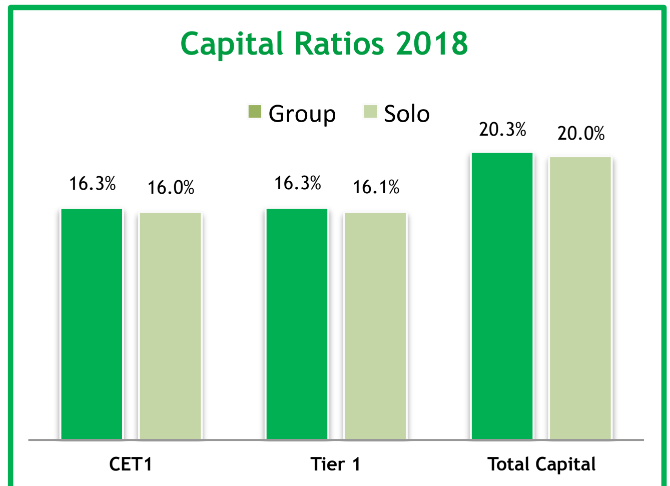
Glossary 60

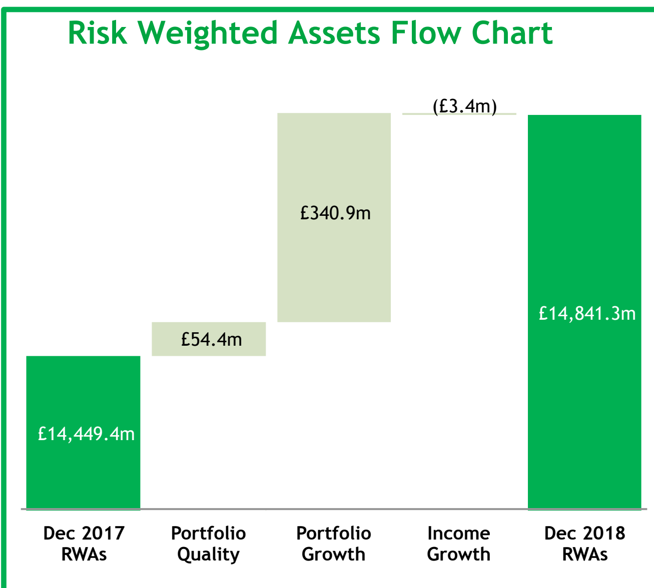
Capital Position at a Glance

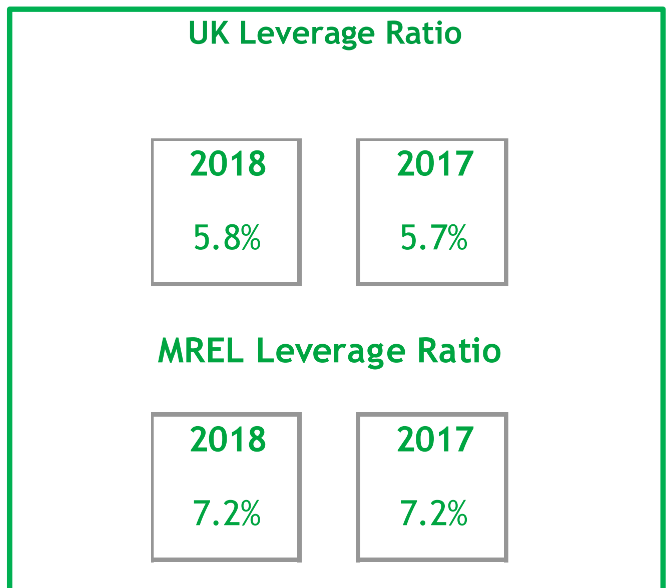












[1] Exposures to Multilateral Development Banks (MDBs), Public Sector Entities (PSEs) and other retail exposures equate to approximately 1% of exposures.

[2] Exposures to central government, central banks, MDBs, PSEs, covered bonds and other retail exposures equate to less than 1% of risk weighted assets.

1 Overview

1.1 Background

This document is prepared under the European Union's Capital Requirements Regulation (CRR) and Capital Requirements Directive (CRD) (together commonly referred to as CRD IV) in place on 31 December 2018.

CRD IV came into force on 1 January 2014 and updates the three "pillars" of the Basel Framework which first came into force on 1 January 2008. Pillar 1 of the standards sets out the minimum capital requirement firms are required to meet for credit, market and operational risk. Under Pillar 2, firms and supervisors have to take a view on whether a firm should hold additional capital against risks not covered in Pillar 1, assess the suitability of Pillar 1 capital requirements and demonstrate their ability to maintain an adequate capital position through a period of stress. Pillar 3 aims to improve market discipline by requiring firms to publish key details of their risks, capital and risk management.

1.2 Basis, policy and frequency of disclosures

This disclosure document has been prepared by Yorkshire Building Society ("the Society") in accordance with the requirements of Pillar 3 set out in Articles 431-455 of the CRR. The Society has adopted the Pillar 1 standardised approach to credit risk, counterparty credit risk and operational risk and does not use any internal models or advanced methods. The Society is also subject to Pillars 2 and 3. The rules are enforced in the United Kingdom (UK) by the Prudential Regulation Authority (PRA).

This document is produced in accordance with the Society's Pillar 3 Disclosure Policy which is reviewed on an annual basis.

Unless otherwise stated, all figures are as at 31 December 2018, the Society's financial year-end and information is shown at a Group level. This document is produced annually and is published at the same time as the Group Annual Report and Accounts.

The Society is currently in the process of applying for permission from the PRA to use the Internal Ratings Based (IRB) approach to calculating capital requirements, see section 1.7 for more details.

1.3 Scope

Yorkshire Building Society is a European Economic Area (EEA) parent institution that is regulated in the UK by the PRA and Financial Conduct Authority (FCA). CRD IV therefore applies to the Society and its subsidiary undertakings.

Consolidation of the Group position for regulatory capital purposes (the "Capital Group") is similar to the statutory consolidated Group position produced for the Group Annual Report and Accounts but differs in the following respects:

- One Group company, Yorkshire Key Services Limited, is no longer trading and is outside of the scope of CRD IV and is therefore not consolidated for capital purposes due to the non-financial nature of its activities, but is fully consolidated in the Group Annual Report and Accounts. The Society's investment in Yorkshire Key Services is neither deducted nor consolidated on grounds of materiality but is risk weighted.
- Some definitions of assets and capital differ between the regulatory capital adequacy rules under CRD IV and the statutory accounting requirements under International Financial Reporting Standards (IFRS); Table 2 gives a detailed reconciliation of statutory accounting capital values to regulatory capital values. The Society applied IFRS 9 from 1

January 2018. Further details of this can be found in section 3.10 and in Note 1 to the Group Annual Report and Accounts.

There are no restrictions or impediments to the movement of capital between legal entities within the Capital Group, and there is no material capital surplus or deficit relating to Group legal entities that do not form part of the Capital Group.

Under CRD IV, Yorkshire Building Society as a legal entity must also meet an individual (solo) consolidated capital requirement. In this area, the Society has made use of provisions laid down in CRD IV to provide capital resources and requirements to the PRA under an individual (solo) consolidated basis. Individual (solo) consolidation enables both the intra-group exposures and investments of the Society in its subsidiaries within the Solo-consolidated Group to be eliminated when calculating capital requirements and the reserves of such subsidiaries to be aggregated with the parent when calculating capital resources.

The entities included under Solo-consolidation in 2018 were:

- Yorkshire Building Society
- Accord Mortgages Limited
- Norwich & Peterborough (LBS) Limited

Further details of the Society's principal subsidiary undertakings are included in Note 10 to the Group Annual Report and Accounts.

1.4 Capital management principles and risk appetite

The Society's management of capital is based on a number of key principles:

- The Society will at all times ensure it holds sufficient capital, of the right quality and stability, to ensure financial sustainability and the security of members' deposits, to support its strategic objectives, to retain the confidence of key external stakeholders and to fulfil its regulatory requirements to maintain a buffer to protect against unexpected losses.
- The Society will seek to utilise its capital resources in an appropriate manner to ensure that the risk / reward balance is optimised and that the Society obtains a suitable return where capital is utilised. This includes seeking to align its regulatory capital needs with its risk capital needs by means of pursuing an application for the IRB approach to calculation of its capital requirements.
- The Society will, as far as possible, seek to ensure an appropriate and efficient mix of capital is available commensurate with its risk profile and strategic ambitions.

The Society considers both risk based capital requirements and non-risk based leverage requirements when determining the Society's capital strategy and has adopted a range of performance metrics over and above the regulatory minimum as the Society's risk appetite.

The Society maintains a management buffer above minimum regulatory requirements of 1.0% of RWAs plus the difference between the current Countercyclical buffer (CCyB) rate and 2.5% (the maximum CCyB rate). As at 31 December 2018, the management buffer was 2.5% of RWAs.

Summarised regulatory capital positions and forecasts (including forecasts under stress scenarios) are reported to the Board and to the Asset and Liability Committee (ALCO). Specific capital management reports are presented to the appropriate executive risk and management committees.

1.5 Location and verification

These disclosures have been reviewed by the Society's Audit Committee on behalf of the Society's Board and are published on the Society's website (www.ybs.co.uk) at the same time as the Group Annual Report and Accounts. The disclosures are not subject to external audit except where they are equivalent to those prepared under accounting requirements for inclusion in the Group Annual Report and Accounts.

1.6 Regulatory Developments

Following the introduction of CRD IV in 2014, there have been a number of regulatory changes as CRD IV becomes fully implemented. The following changes have had an impact on the Society in 2018:

- The Society is required to hold a Countercyclical Capital Buffer, which increased to 1% of RWAs in November 2018.
- The European Commission released a combined package of proposals (CRD V/CRR II) introducing the Net Stable Funding Ratio (NSFR) and the Leverage Ratio as binding requirements for EU banks, as well as revisions to counterparty credit risk. The expectation is that these proposals will be finalised in the first half of 2019.

1.7 Recent Developments

During 2018, the Society applied to the PRA for permission to apply the IRB approach to calculating capital requirements. This is a modular (three phase) application process and the PRA are currently reviewing the second phase of the application.

2 Capital Resources

2.1 Total Available Capital

As at 31 December 2018, and throughout the year, the Society complied with the capital requirements that were in force as set out by European Union and UK legislation. The following table shows the breakdown of the total available capital for the Capital Group and Solo-consolidated Group as at 31 December 2018.

Table 1 - Capital Resources	Group 2018	Group 2017	Solo 2018	Solo 2017
	£m	£m	£m	£m
Common Equity Tier 1 (CET1)				
General reserve	2,518.5	2,377.2	2,478.7	2,361.5
Fair value through other comprehensive income reserve	6.2	10.8	6.2	10.8
Cash flow hedge reserve	(1.8)	(3.6)	(1.8)	(3.6)
CET1 regulatory adjustments				
Prudent valuation adjustment	(2.3)	(1.6)	(2.1)	(1.3)
Pension scheme adjustment	(56.9)	(71.4)	(56.9)	(71.4)
Intangible fixed assets	(39.8)	(31.3)	(39.8)	(31.3)
Securitisation holdings deducted from capital resources	(3.2)	-	(3.2)	-
Cash flow hedge reserve	1.8	3.6	1.8	3.6
IFRS 9 transitional arrangements	0.4	-	0.4	-
Total CET1	**2,422.9**	**2,283.7**	**2,383.3**	**2,268.3**
Additional Tier 1 Capital				
Permanent Interest Bearing Shares (PIBS)	2.5	3.2	2.5	3.2
Total Tier 1 capital	**2,425.4**	**2,286.9**	**2,385.8**	**2,271.5**
Tier 2 Capital				
Subordinated liabilities	585.1	589.2	585.1	589.2
Collective provisions for impairment	-	24.5	-	24.5
Total Tier 2 capital	**585.1**	**613.7**	**585.1**	**613.7**
Total capital available	**3,010.5**	**2,900.6**	**2,970.9**	**2,885.2**

2.2 Tier 1 Capital

2.2.1 Common Equity Tier 1 Capital

CET1 capital resources comprises the general reserve, fair value through other comprehensive income reserve and adjustments for items reflected in the general reserve which are treated separately for capital adequacy purposes. The following items are fully deducted under CRD IV:

- A Prudent Valuation Adjustment (PVA) is applied to fair-valued positions and is deducted from CET1 capital as per CRD IV. As at 31 December 2018, the net impact of the PVA was a reduction in CET1 capital of £2.3m.

- Defined benefit pension fund assets are deducted from CET1 capital resources, net of any associated deferred tax liabilities. As at 31 December 2018, the net impact of the adjustment was a reduction in CET1 capital of £56.9m.
- An adjustment is also made in respect of intangible fixed assets. For accounting purposes, items including software development costs, other intangibles resulting from business combinations and goodwill are capitalised as intangible fixed assets where they meet certain criteria. Intangibles are deducted from capital under the regulatory rules.

  As at 31 December 2018, the deduction amounted to £39.8m.
- Securitisation positions (including resecuritisations) that are unrated or have low external ratings can be risk weighted at 1,250% or deducted from CET1 capital under CRD IV. The policy used by the Society is to deduct this, as in the above table. This exposure relates to a legacy position that was previously written down to zero.
- The cash flow hedge reserve does not form part of regulatory capital, net of associated deferred tax.
- Following the implementation of IFRS 9, any increase in impairment provisions may be added back to CET1 capital resources on a reducing basis, over five years. Currently 95% of the increase in provisions is added back to CET1.

  As at 31 December 2018 this amounted to £0.4m.

  Further details on IFRS 9 Transitional Arrangements can be found in Section 3.10.

2.2.2 Additional Tier 1 Capital

Additional Tier 1 Capital comprises of Permanent Interest Bearing Shares (PIBS). PIBS are unsecured deferred shares and rank behind the claims of subordinated noteholders, depositors, creditors and investing members of the Society. Further details about PIBS are provided in Note 30 to the Group Annual Report and Accounts and full terms and conditions of the Society's PIBS can be found on the Society's website:

http://www.ybs.co.uk/your-society/treasury/wholesale_funding/subordinated-debt-info.html

Under CRD IV these instruments are being phased out over a ten year period. Currently 40% of the PIBS balance sheet carrying value qualifies as Tier 1 capital.

2.3 Tier 2 Capital

Tier 2 Capital comprises the Society's qualifying subordinated liabilities. Following the implementation of IFRS 9, the collective allowances for impairment no longer exists.

Subordinated notes are unsecured and rank behind the claims of all depositors, creditors and investing members (other than holders of PIBS) of the Society. For regulatory capital purposes, the value of any subordinated liabilities is amortised in the last five years to maturity. More details of the subordinated liabilities are included in Note 29 to the Group Annual Report and Accounts and the full terms and conditions of the Society's subordinated liabilities can be found on the Society's website:

http://www.ybs.co.uk/your-society/treasury/wholesale_funding/subordinated-debt-info.html

2.4 Reconciliation of Regulatory Capital to Balance Sheet Capital

The table below shows how the balance sheet capital values in the Group Annual Report and Accounts reconcile to the regulatory capital equivalent for the Society at as 31 December 2018.

Table 2 - Reconciliation of Accounting Capital to Regulatory Capital	Accounting Balance Sheet Capital Value £m	Adjustments to Balance Sheet Capital Value £m	Regulatory Capital Value £m	Ref
CET1				
Total equity attributable to members	2,528.4			1
Less reserves not included in regulatory capital:				
Non-consolidated subsidiary		(5.5)		4
Total adjustments to Common Equity Tier 1 resources		**(5.5)**		
CET1	**2,528.4**	**(5.5)**	**2,522.9**	
CET1 Regulatory Adjustments				
Prudent Valuation Adjustment		(2.3)		2
Pension Scheme Adjustment		(56.9)		2
Intangible fixed assets		(39.8)		2
Securitisation holdings deducted from capital resources		(3.2)		2
Deferred tax assets that rely on future profitability		-		2
Cash flow hedge reserve		1.8		
IFRS 9 transitional arrangements		0.4		
Total regulatory adjustments to Common Equity Tier 1 capital		**(100.0)**		
Total CET1	**2,528.4**	**(105.5)**	**2,422.9**	
Additional Tier 1 capital				
Subscribed capital (Permanent Interest Bearing Shares)	6.1			1
Adjustment to phase out subscribed capital		(3.6)		
Total Additional Tier 1 capital	**6.1**	**(3.6)**	**2.5**	3
Total Tier 1 capital after deductions	**2,534.5**	**(109.1)**	**2,425.4**	
Tier 2 capital				
Subordinated Liabilities	585.1	0.0	585.1	1
Tier 2 capital after deductions	**585.1**	**0.0**	**585.1**	
Total capital resources after deductions	**3,119.6**	**(109.1)**	**3,010.5**	

[1] Statement of Financial Position, Group Annual Report and Accounts

[2] Pillar 3 Disclosures, Table 1

[3] As per 2.2.2 above only 40% of PIBS balance sheet carrying value qualifies as Tier 1 capital

[4] See section 1.3 for further details

2.5 Capital Flow Statement

The table below shows the flow of Group regulatory capital and associated deductions in 2018.

Table 3 - Regulatory Capital Flow Statement	2018 £m	Ref
Total CET1 Capital		
1 January 2018	2,283.7	
Total comprehensive income in 2018	134.5	1
IFRS 9 transition adjustments	4.0	
Profits allocated to hedging reserve	(1.9)	2
Change in Prudent Valuation Adjustment	(0.6)	
Change in pension scheme adjustment	14.5	
Change in intangible fixed assets	(8.5)	
Change in securitisation holdings deducted from capital resources	(3.2)	
Change in IFRS 9 transitional arrangements	0.4	
Total CET1 Capital as at 31 December 2018	**2,422.9**	
Additional Tier 1 capital		
1 January 2018	3.2	
Movement in market valuation of PIBS and eligible percentage	(0.7)	
Additional Tier 1 capital as at 31 December 2018	**2.5**	
Total Tier 1 capital as at 31 December 2018	**2,425.4**	
Tier 2 Capital		
1 January 2018	613.7	
Issuance of Tier 2 Capital	-	
Maturity of Tier 2 Capital	(0.5)	
Amortisation and other adjustments	(3.6)	
Movement in collective provisions for impairment	(24.5)	
Tier 2 capital before deductions as at 31 December 2018	**585.1**	
Total capital available as at 31 December 2018	**3,010.5**	

[1] Statement of Comprehensive Income, Group Annual Report and Accounts

[2] Statement of Changes in Member's Interest, Group Annual Report and Accounts

3 Capital Requirements

3.1 Overview

Regulatory capital covers the following risks across the Capital Group:

- Pillar 1 risks (i.e. credit risk, counterparty credit risk and operational risk). The minimum capital requirement is calculated using regulatory-prescribed risk weightings. The Society has adopted the standardised approach to both credit and operational risk in order to calculate the Pillar 1 minimum capital requirement.
- Pillar 2A risks (i.e. all other material risks which are not adequately captured or captured at all under Pillar 1). Each material risk that the Society has identified outside the scope of Pillar 1 (e.g. pension obligation risk, interest rate risk, concentration risk) has undergone considered and vigorous stress testing to calculate an economic value for each of the material risks across the Society where capital is an appropriate mitigant, and are documented in the Internal Capital Adequacy Assessment Process (ICAAP) document (see section 3.13 below). See section 3.6 below for the Society's total Pillar 1 and Pillar 2A capital requirements.
- Capital Conservation Buffer. The Society calculates a Capital Conservation Buffer (CCB) as specified in CRD IV. The CCB is calculated as a percentage of RWAs, set at 1.875% throughout 2018. The CCB increased to 2.5% of RWAs on 1 January 2019.
- PRA Buffer. The Society may need to hold an additional capital requirement (in addition to the Pillar 1 and Pillar 2A amounts above) representing the amount by which the Society's capital surplus would reduce in a "severe but plausible" stress scenario over the Society's planning horizon – known as the Capital Planning Stress Test. This additional requirement is known as the PRA buffer and does not form part of the overall regulatory total capital requirement. This stress test is defined and articulated with the assistance of key business experts and is set at a severity level that is consistent with the PRA's "severe but plausible" requirement. The result of this stress test is compared to the CCB and an additional PRA Buffer held where the CCB is not considered sufficient to cover the risks in the scenario.

  The PRA Buffer can, in extreme times of stress, be utilised without breaching the regulatory minimum.
- Countercyclical Buffer (CCyB). The Society is required to hold a Countercyclical Buffer which was introduced to ensure financial institutions hold more capital in favourable economic conditions so it can be utilised in economic downturns. This buffer is currently 1% of RWAs.

3.2 Pillar 1

The following tables show the credit and operational risk exposure, average risk weight and RWAs for each of the Society's exposure classes and the resultant Pillar 1 minimum capital requirements (being 8% of RWAs).

- The exposure is based on the definitions for regulatory capital purposes, before impairment provision and credit risk mitigation such as collateral held and government guarantees.
- After the impairment provision and credit risk mitigation adjustment, the Retail (current accounts and personal loans) capital exposure is reduced to nil, therefore showing an average RW of 0%.
- Credit Valuation Adjustment (CVA) RWAs are included in the Financial Institutions line, increasing the average risk weight.
- Capital requirements and RWAs for operational risk are shown; however, as they do not relate to asset exposures they do not have an exposure value.

- £3.2m of securitisation exposure is deducted from capital resources, rather than it being assigned a risk weighting of 1,250%. This exposure relates to a legacy position that was previously written down to zero.

Table 4a - Pillar 1 Capital Requirement - Group 2018	Exposure	RWAs	Capital Requirements	Average Risk Weight
	£m	£m	£m	%
Loans secured by mortgages on immovable property				
Loans to individuals	36,431.6	12,911.7	1,032.9	35.5%
Commercial lending (excluding SME)	175.1	175.0	14.0	100.0%
Commercial lending (SME)	385.8	293.6	23.5	76.2%
Past due (three months or more)	136.9	127.7	10.2	100.2%
Immovable property total	**37,129.4**	**13,508.0**	**1,080.6**	**36.4%**
Wholesale exposure classes				
Securitisation positions	3.5	0.2	0.0	4.9%
Central governments or central banks	11,902.4	-	-	0.0%
Covered bonds	309.1	30.9	2.5	10.0%
Financial institutions	1,166.7	391.0	31.3	52.5%
Multilateral Development Banks	194.8	-	-	0.0%
Public Sector Entities	219.5	-	-	0.0%
Short term claims on financial institutions and corporates	139.8	28.0	2.2	20.0%
Wholesale total	**13,935.8**	**450.1**	**36.0**	**5.6%**
Retail				
Current accounts	0.5	-	-	n/a
Personal loans	0.6	-	-	n/a
Retail total	**1.1**	**-**	**-**	**n/a**
Operational risk	n/a	699.6	56.0	n/a
Other assets	287.2	183.6	14.7	63.9%
Total	**51,353.5**	**14,841.3**	**1,187.3**	**32.7%**

Table 4b - Pillar 1 Capital Requirement - Group 2017	Exposure £m	RWAs £m	Capital Requirements £m	Average Risk Weight %
Loans secured by mortgages on immovable property				
Loans to individuals	35,226.1	12,490.1	999.2	35.5%
Commercial lending (excluding SME)	142.2	141.6	11.4	100.0%
Commercial lending (SME)	375.7	285.3	22.8	76.2%
Past due (three months or more)	158.6	150.6	12.0	100.8%
Immovable property total	**35,902.6**	**13,067.6**	**1,045.4**	**36.4%**
Wholesale exposure classes				
Securitisation positions	3.9	8.7	0.7	225.0%
Central governments or central banks	13,918.2	-	-	0.0%
Covered bonds	-	-	-	-
Financial Institutions	2,406.1	432.8	34.6	70.9%
Multilateral Development Banks	38.9	-	-	0.0%
Public Sector Entities	80.2	-	-	0.0%
Short term claims on financial institutions and corporates	245.1	49.0	3.9	20.0%
Wholesale total	**16,692.4**	**490.5**	**39.2**	**5.3%**
Retail				
Current accounts	1.0	-	-	n/a
Personal loans	1.0	-	-	n/a
Retail total	**2.0**	**-**	**-**	**n/a**
Operational risk	n/a	703.1	56.2	n/a
Other assets	302.5	188.2	15.2	62.2%
Total	**52,899.5**	**14,449.4**	**1,156.0**	**31.9%**

Table 4c - Pillar 1 Capital Requirement - Solo 2018	Exposure £m	RWAs £m	Capital Requirements £m	Average Risk Weight %
Loans secured by mortgages on immovable property				
Loans to individuals	36,431.6	12,911.7	1,032.9	35.5%
Commercial lending (including SME)	175.1	175.0	14.0	100.0%
Commercial lending (SME)	385.8	293.6	23.5	76.2%
Past due (three months or more)	136.9	127.7	10.2	100.2%
Immovable property total	**37,129.4**	**13,508.0**	**1,080.6**	**36.4%**
Wholesale exposure classes				
Securitisation positions	3.5	0.2	0.0	4.9%
Central governments or central banks	11,902.4	-	-	0.0%
Covered bonds	309.1	30.9	2.5	10.0%
Financial institutions	1,166.7	391.0	31.3	52.5%
Multilateral Development Banks	194.8	-	-	0.0%
Public Sector Entities	219.5	-	-	0.0%
Short term claims on financial institutions and corporates	139.6	27.9	2.2	20.0%
Wholesale total	**13,935.6**	**450.0**	**36.0**	**5.6%**
Retail				
Current accounts	0.5	-	-	n/a
Personal loans	0.6	-	-	n/a
Retail total	**1.1**	**-**	**-**	**n/a**
Operational risk	n/a	680.6	54.4	n/a
Other assets	2,655.9	216.6	17.4	8.2%
Total	**53,722.0**	**14,855.2**	**1,188.4**	**31.1%**

Table 4d - Pillar 1 Capital Requirement - Solo 2017	Exposure £m	RWAs £m	Capital Requirements £m	Average Risk Weight %
Loans secured by mortgages on immovable property				
Loans to individuals	35,226.1	12,490.1	999.2	35.5%
Commercial lending (excluding SME)	142.2	141.6	11.4	100%
Commercial lending (SME)	375.7	285.3	22.8	76.2%
Past due (three months or more)	158.6	150.6	12.0	100.8%
Immovable property total	**35,902.6**	**13,067.6**	**1,045.4**	**36.4%**
Wholesale exposure classes				
Securitisation positions	3.9	8.7	0.7	225.0%
Central governments or central banks	13,918.2	-	-	0.0%
Covered bonds	-	-	-	-
Financial institutions	2,406.1	432.8	34.6	70.9%
Multilateral Development Banks	38.9	-	-	0.0%
Public Sector Entities	80.2	-	-	0.0%
Short term claims on financial institutions and corporates	244.9	49.0	3.9	20.0%
Wholesale total	**16,692.2**	**490.5**	**39.2**	**5.3%**
Retail				
Current accounts	1.0	-	-	n/a
Personal loans	1.0	-	-	n/a
Retail total	**2.0**	**-**	**-**	**n/a**
Operational risk	n/a	710.9	56.9	n/a
Other assets	2,937.8	220.8	17.7	7.5%
Total	**55,534.6**	**14,489.8**	**1,159.2**	**30.2%**

3.3 Capital Adequacy

The table below summarises the Society's capital adequacy position, using key figures from Tables 1, 9 and 10.

Table 5 - Capital Adequacy	Group 2018	Group 2017	Solo 2018	Solo 2017
	£m / %	£m / %	£m / %	£m / %
Capital Excess				
Total pillar 1 capital requirement	1,187.3	1,156.0	1,188.4	1,159.2
Total capital resources	3,010.5	2,900.6	2,970.9	2,885.2
Excess of own funds over minimum pillar 1 requirement	**1,823.2**	**1,744.6**	**1,782.5**	**1,726.0**
Total risk weighted assets	14,841.3	14,449.4	14,855.2	14,489.8
Common Equity Tier 1 capital resources	2,422.9	2,283.7	2,383.3	2,268.3
Tier 1 capital resources	2,425.4	2,286.9	2,385.8	2,271.5
Total capital resources	**3,010.5**	**2,900.6**	**2,970.9**	**2,885.2**
Common Equity Tier 1 capital ratio	16.3%	15.8%	16.0%	15.7%
Tier 1 capital ratio	16.3%	15.8%	16.1%	15.7%
Total capital ratio/MREL capital ratio	20.3%	20.1%	20.0%	19.9%
UK Leverage Ratio	5.8%	5.7%	4.9%	4.9%
CRR Leverage Ratio	5.4%	5.1%	4.6%	4.4%
MREL Leverage Ratio	7.2%	7.2%	6.1%	6.2%

Sections 5 and 6 provide further detail on the significant risks captured under Pillar 1, i.e. credit risk and operational risk, including the nature of the exposures and the key risk management techniques. A summary of other significant risks captured under Pillar 2 is contained in section 7.

Given the total minimum capital requirements are not materially different on a Group or Solo consolidated basis, the disclosures in the remainder of this document are on a Group basis.

3.4 RWA Flow Statement

The table below shows the causes of movements in RWAs in the year at the Group level. In the table below, operational risk has been included to fully illustrate overall RWA movements. Changes in operational risk requirements reflect income growth within the regulatory prescribed income streams.

Table 6 - RWA Flow Statement (Group)	2017 RWAs	Portfolio Quality	Portfolio Growth	Income Growth	2018 RWAs
	£m	£m	£m	£m	£m
Loans secured on immovable property	13,067.6	(8.3)	448.7	-	13,508.0
Wholesale credit risk	490.5	62.7	(103.1)	-	450.1
Retail credit risk	-	-	-	-	-
Other credit risk	188.2	-	(4.6)	-	183.6
Operational risk	703.1	-	-	(3.5)	699.6
Total risk weighted assets	**14,449.4**	**54.4**	**341.0**	**(3.5)**	**14,841.3**

3.5 Pillar 2A

In January 2018 (following a Periodic Summary Meeting), the PRA confirmed the Society's Pillar 2A requirement as 0.63% of RWAs compared to 2.3% of RWA as at 31 December 2017. The decrease in Pillar 2A requirement is as a result of the implementation of PS22/17 – Refining the PRA's Pillar 2A Capital Framework.

3.6 Total Capital Requirement

The Society's Total Capital Requirement (Pillar 1 + Pillar 2A) as at 31 December 2018 is £1,278.3m which is equivalent to 8.6% of RWAs.

The table below details the Society's Pillar 1 and Pillar 2A requirement.

Table 7 - Total Capital Requirement	2018		2017	
	£m	% of RWAs	£m	% of RWAs
Pillar 1 requirement	1,187.3	8.0%	1,156.0	8.0%
Pillar 2A requirement	91.0	0.6%	327.0	2.3%
Total Capital Requirement (TCR)	**1,278.3**	**8.6%**	**1,483.0**	**10.3%**

3.7 Regulatory Capital Buffers

The table below details the regulatory capital buffers applicable to the Society, it does not include the PRA buffer which is a firm specific buffer set by the PRA; the PRA requires that this buffer is not publicly disclosed.

Table 8 - Regulatory Capital Buffers	2018		2017	
	£m	% of RWAs	£m	% of RWAs
Capital Conservation Buffer	278.3	1.88%	181.0	1.25%
Countercyclical Capital Buffer	148.4	1.00%	0.0	0.00%
Total Regulatory Buffer requirement	426.7	2.88%	181.0	1.25%

3.8 Leverage Ratio

This is a non-risk based requirement that measures the relationship between capital resources and an adjusted measure of total on and off-balance sheet assets. This requirement only applies to financial institutions with greater than £50bn of deposits; the Society is currently not captured under this approach.

The UK leverage ratio is calculated as:

$$\frac{\text{Tier 1 Capital}}{\text{Total on and off-balance sheet assets (applying regulatory adjustments)}}$$

The table below shows the leverage ratio calculation with balance sheet assets excluding assets constituting as claims on central banks.

Table 9 - UK Leverage Ratio	Group 2018 £m / %	Group 2017 £m / %
Tier 1 Resources	2,425.4	2,286.9
Leverage Exposure	41,760.7	40,294.0
Leverage Ratio %	**5.8%**	**5.7%**

The table below shows the leverage ratio calculation as per the CRR.

Table 10 - CRR Leverage Ratio	Group 2018 £m / %	Group 2017 £m / %
Balance Sheet Assets	**43,049.2**	**42,041.7**
Regulatory Adjustments		
Mortgage pipeline	293.4	678.0
Other committed facilities	32.1	19.9
Repurchase agreements	2,068.2	2,640.8
Netted derivatives adjustment	(144.2)	(151.3)
Tier 1 deductions	(100.0)	(104.3)
Leverage Ratio Assets	**45,198.7**	**45,124.8**
Tier 1 Capital Resources	**2,425.4**	**2,286.9**
Leverage Ratio %	**5.4%**	**5.1%**

3.9 Minimum Requirement for Eligible Liabilities (MREL)

The table below shows the Society's progress in meeting MREL requirements on both a transitional and end-state basis prior to the addition of applicable buffers. The Society will be subject to the lower of the transitional MREL requirements (18% of risk weighted assets) or the end state requirements (double pillar 1 and 2A) plus applicable buffers from 1st January 2020.

If MREL rules had been in place as at 31 December 2018, the Society's MREL requirement would be based on the end state requirements.

The Society anticipates that its MREL requirement on 1 January 2020 will also be based on the end-state requirements.

The Society is well positioned to meet the MREL requirements in 2020 through retained profits and further issuance of qualifying MREL instruments. Whilst there is a risk that a disorderly Brexit may impact on the ability to issue debt at a reasonable coupon, the Society is highly confident that this risk can be comfortably managed with alternative action taken if required, including reducing planned business growth.

Table 11a - The Society's progress to meeting MREL requirements	2018			2017		
	£m	% of RWAs	% of Leverage Exposure	£m	% of RWAs	% of Leverage Exposure
Transitional Requirements	2,671.4	18.0%	6.4%	2,600.9	18.0%	6.5%
End-state Capital Requirements[1]	2,556.6	17.2%	6.1%	2,966.0	20.5%	7.4%
End-state Leverage Requirements[2]	2,714.4	18.3%	6.5%	2,619.1	18.1%	6.5%
Total Capital Resources	**3,010.5**	**20.3%**	**7.2%**	**2,900.6**	**20.1%**	**7.2%**

Table 11b - MREL - Total liabilities and Own Funds	2018	2017
	%	%
MREL Resources / (Total Liabilities plus Own Funds)	7.0%	6.9%
End-state Capital Requirements[1]/ (Total Liabilities plus Own Funds)	6.0%	7.1%
End-state Leverage Requirements[2] / (Total Liabilities plus Own Funds)	6.3%	6.2%

[1] The End-state capital requirement provided is equal to Pillar 1 plus Pillar 2A doubled.

[2] The End-state leverage requirement provided is equal to the minimum leverage requirement doubled (calculated as per PS21/17).

3.10 IFRS 9 - Impact of Transitional Arrangements

Under EU Regulation 2017/2395, the Society is permitted to apply transitional arrangements, which allows relief to capital ratios to reduce the impact of the implementation of IFRS 9.

The below table shows the impact of IFRS 9 transitional arrangements as at 31 December 2018.

Table 12 - IFRS 9 Transitional arrangements impact	IFRS 9 Full Impact	IFRS 9 Transitional arrangements
	£m	£m
Capital Resources		
CET1 capital	2,422.5	2,422.9
Tier 1 capital	2,425.0	2,425.4
Total Capital	**3,010.1**	**3,010.5**
RWA	14,840.8	14,841.3
UK Leverage exposure	41,760.3	41,760.7
CRR Leverage exposure	45,198.3	45,198.7
Capital Ratios		
CET1 ratio	16.3%	16.3%
Tier 1 ratio	16.3%	16.3%
Total capital ratio	20.3%	20.3%
UK Leverage ratio	5.8%	5.8%
CRR Leverage ratio	5.4%	5.4%

Further details of the impact of IFRS 9 can be found in the Group Annual Report and Accounts, included in Note 1.

3.11 Stress Testing Results

Although the Society is not currently part of the Bank of England's concurrent stress testing regime; as part of its annual Capital Planning Stress Test, the Society undertook the Bank of England's 2018 stress test scenario based on results as at December 2017. This featured deep simultaneous recessions both globally and in the UK combined with falling house prices and escalating conduct costs. In the scenario, UK GDP falls by 4.7%; UK unemployment rises to 9.5% and residential property prices in the UK fall by 33%.

At all times throughout the stress, the Society's CET1 ratio (before management actions) remained above both stressed and normal risk appetite, as well as regulatory requirements, meaning the Society would be able to continue with its lending plans even in a severe stress scenario.

It was deemed that no management actions would be necessary to mitigate the impact of the stress.

Table 13 - Projected ratios in the 2018 BoE stress scenario	2017	Minimum stressed ratio before 'strategic' management actions
	%/£m	%/£m
IFRS 9 Transitional		
CET1 Ratio	15.8%	14.8%
Tier 1 Ratio	15.8%	14.8%
Total Capital Ratio	19.9%	16.9%
Leverage Ratio	5.7%	6.4%
IFRS 9 Non-Transitional		
CET1 Ratio	15.8%	14.6%
Leverage Ratio	5.7%	6.3%

In amongst the frequent stress testing activity undertaken for both regulatory and risk management purposes, the Society has also run testing in line with the Bank of England's disorderly Brexit scenario. The results of this stress testing showed that the Society would not face capital issues in such a scenario.

3.12 Impact of CRD IV

This section is intended to assist in understanding how the implementation of CRD IV will affect the Society's capital position. The table below shows the capital position under CRD IV rules as they stand under PRA national implementation, and on a final rules basis (applying the final CRD IV rules without transitional elements, as the rules will stand in 2022). All figures are as at 31 December 2018.

Table 14 - CRD IV Capital Position	Transitional	Final Rules
	£m	£m
Common Equity Tier 1 (CET1)		
General reserve	2,518.5	2,518.5
Regulatory adjustments:		
Fair value through other comprehensive income reserve	6.2	6.2
Cash flow hedge reserve	(1.8)	(1.8)
Pension scheme adjustment	(56.9)	(56.9)
CET1 deductions:		
Prudent Valuation Adjustment	(2.3)	(2.3)
Intangible fixed assets	(39.8)	(39.8)
Securitisation holdings deducted from capital resources	(3.2)	(3.2)
IFRS 9 transitional arrangements	0.4	0.4
Cash flow hedge reserve	1.8	1.8
Total CET1 capital	**2,422.9**	**2,422.9**
Additional Tier 1 (AT1) Capital		
Permanent Interest Bearing Shares (PIBS)	2.5	-
Total Tier 1 capital	**2,425.4**	**2,422.9**
Tier 2 (T2) Capital		
Subordinated liabilities	585.1	585.1
Total Tier 2 capital	**585.1**	**585.1**
Total capital Resources	**3,010.5**	**3,008.0**
Total RWAs	**14,841.3**	**14,841.3**
CET1 Ratio	16.3%	16.3%
Tier 1 Ratio	16.3%	16.3%
Total Capital Ratio	20.3%	20.3%
Leverage Ratio (UK framework)	5.8%	5.8%
Leverage Ratio (CRR framework)	5.4%	5.4%
MREL Leverage Ratio	7.2%	7.2%

3.13 Internal Capital Adequacy Assessment Process (ICAAP)

The Society undertakes the ICAAP at least annually, which is an internal assessment of its capital requirement. In performing the ICAAP, the Society considers the key risks, to which it is exposed, and the levels of capital and other financial resources that should be held to safeguard the interests of its members and depositors, particularly during times of stress.

This process includes:

- Identification by senior managers of the relevant risk categories for the Society.
- Establishment, under the sponsorship of senior management, of separate work streams to consider each risk category in detail.
- Analysis of the risks within each work stream, involving relevant personnel from across the business, with this being documented in individual risk assessment documents.
- Consideration of whether capital is an appropriate mitigant to the risk. Where this is deemed to be the case, capital requirements are calculated based on the results of stress testing for each risk category. Where capital is not deemed appropriate to mitigate a particular risk, alternative management actions are identified and described within the risk assessment. For certain risks where capital is not an appropriate mitigant, the holding of liquidity can be used to mitigate the risk. In these cases, the risk is considered in more depth as part of the Individual Liquidity Adequacy Assessment Process (ILAAP).
- Approval of individual risk assessment documents by the relevant sponsor and committee.
- Calculation of an appropriate PRA Buffer to absorb a “severe but plausible” economic stress event over the Society’s planning horizon, should such a scenario materialise, thereby ensuring minimum capital requirements are maintained.
- Documentation of the overall process.
- The final assessment is presented to Asset and Liability Committee (ALCO) and Executive Risk Committee (ERC) before being presented to Group Risk Committee (GRC) and the Board (with whom ultimate responsibility lies) for challenge and approval.

Further information on the material risks identified as part of the ICAAP can be found in sections 5, 6 and 7 of this document.

4 Risk Management

The activities of financial institutions inevitably involve a degree of risk taking. The Society's ability to properly identify, measure, monitor and report risk is critical to its soundness and its ability to provide value and fair outcomes to its membership and customers. The Society's risk management framework and governance structures are intended to provide appropriate and comprehensive monitoring, control and ongoing management of the major risks to which the Society is exposed. These are fully set out in the Strategic Report and the Risk Management Report in the Group Annual Report and Accounts.

5 Credit Risk

5.1 Credit Risk Overview

Credit risk is the potential risk of financial loss arising from the failure of a customer or other counterparty to settle their financial and contractual obligations as they fall due.

For the purposes of Pillar 3 disclosures, credit risk is sub-divided into loans secured by mortgages on immovable property, wholesale (treasury) and retail (current accounts & personal loans). Details of the Society's risk management and governance practices can be found in the Risk Management Report in the Group Annual Report and Accounts, with further details of exposures included in Notes 38 and 39.

5.2 Credit Risk Exposures

The gross credit risk exposure (based on the definitions for regulatory capital purposes, before impairment provision and credit risk mitigation such as collateral held and government guarantees) and the average for the year is summarised as follows:

Table 15 - Credit Risk Exposure	Average during 2018	Dec 2018	Average during 2017	Dec 2017
	£m	£m	£m	£m
Loans secured by mortgages on immovable property				
Loans to individuals	35,990.0	36,567.2	34,729.0	35,382.9
Commercial lending (including SME)	553.8	562.2	504.0	519.7
Total loans secured on immovable property exposure	**36,543.8**	**37,129.4**	**35,233.0**	**35,902.6**
Wholesale				
Securitisation positions	3.0	3.5	14.3	3.9
Central governments or central banks	12,964.4	11,902.4	12,539.2	13,918.2
Covered bonds	77.4	309.1	-	-
Financial institutions	1,439.5	1,166.7	1,496.3	2,406.1
Multilateral Development Banks	191.2	194.8	16.1	38.9
Public Sector Entities	146.4	219.5	25.6	80.2
Short term claims on institutions and corporates	171.0	139.8	247.9	245.1
Total wholesale exposure	**14,992.9**	**13,935.8**	**14,339.4**	**16,692.4**
Retail				
Current accounts	0.7	0.5	1.2	1.0
Personal loans	0.8	0.6	1.2	1.0
Total retail exposure	**1.5**	**1.1**	**2.4**	**2.0**
Other assets exposure	289.3	287.2	251.8	302.5
Total credit risk exposure	**51,827.5**	**51,353.5**	**49,826.6**	**52,899.5**

The section below gives a detailed breakdown of the material risk categories. A further geographical analysis of loans secured by mortgages on immovable property is disclosed in Note 39 to the Group Annual Report and Accounts.

The geographical distribution of the Society's exposures is as follows.

Table 16a - Credit Risk Exposure - Geographic Distribution 2018	UK	Other European Countries	North America	Rest of the World	Total
	£m	£m	£m	£m	£m
Loans secured by mortgages on immovable property					
Loans to individuals	36,537.4	29.8	-	-	36,567.2
Commercial lending (including SME)	562.2	-	-	-	562.2
Total loans secured on immovable property	**37,099.6**	**29.8**	**-**	**-**	**37,129.4**
Wholesale					
Securitisation positions	-	0.4	-	3.1	3.5
Central governments or central banks	11,902.4	-	-	-	11,902.4
Covered bonds	309.1	-	-	-	309.1
Financial institutions	851.0	293.9	21.7	0.1	1,166.7
Multilateral Development Banks	-	194.8	-	-	194.8
Public sector entities	-	219.5	-	-	219.5
Short-term claims on institutions and corporates	87.0	8.4	44.4	-	139.8
Total wholesale credit exposure	**13,149.5**	**717.0**	**66.1**	**3.2**	**13,935.8**
Total credit risk exposure (excl. retail and other assets)	**50,249.1**	**746.8**	**66.1**	**3.2**	**51,065.2**

Table 16b - Credit Risk Exposure - Geographic Distribution 2017	UK	Other European Countries	North America	Rest of the World	Total
	£m	£m	£m	£m	£m
Loans secured by mortgages on immovable property					
Loans to individuals	35,347.5	35.4	-	-	35,382.9
Commercial lending (including SME)	519.7	-	-	-	519.7
Total loans secured on immovable property	**35,867.2**	**35.4**	**-**	**-**	**35,902.6**
Wholesale					
Securitisation positions	-	3.9	-	-	3.9
Central governments or central banks	13,918.2	-	-	-	13,918.2
Covered bonds	-	-	-	-	-
Financial institutions	829.2	566.9	764.0	246.0	2,406.1
Multilateral Development Banks	-	38.9	-	-	38.9
Public Sector Entities	-	80.2	-	-	80.2
Short-term claims on institutions and corporates	138.7	0.2	106.2	-	245.1
Total wholesale credit exposure	**14,886.1**	**690.1**	**870.2**	**246.0**	**16,692.4**
Total credit risk exposure (excl. retail and other assets)	**50,753.3**	**725.5**	**870.2**	**246.0**	**52,595.0**

The residual maturity of exposures is as follows.

Table 17a - Credit Risk Exposure - Residual Maturity 2018	Up to 12 months	1 to 5 years	5 to 10 years	> than 10 years	Total
	£m	£m	£m	£m	£m
Loans secured by mortgages on immovable property					
Loans to individuals	322.8	991.6	3,064.6	32,188.2	36,567.2
Commercial lending (including SME)	11.3	17.8	73.1	460.0	562.2
Total loans secured on immovable property	**334.1**	**1,009.4**	**3,137.7**	**32,648.2**	**37,129.4**
Wholesale					
Securitisation positions	-	-	-	3.5	3.5
Central governments or central banks	3,530.0	-	753.2	7,619.2	11,902.4
Covered bonds	-	231.9	77.2	-	309.1
Financial institutions	32.1	370.2	575.0	189.4	1,166.7
Multilateral Development Banks	-	169.2	25.6	-	194.8
Public Sector Entities	-	149.2	70.3	-	219.5
Short-term claims on institutions and corporates	139.8	-	-	-	139.8
Total wholesale exposure	**3,701.9**	**920.5**	**1,501.3**	**7,812.1**	**13,935.8**
Total credit risk exposure (excl. retail and other assets)	**4,036.0**	**1,929.9**	**4,638.9**	**40,460.4**	**51,065.2**

Table 17b - Credit Risk Exposure - Residual Maturity 2017	Up to 12 months	1 to 5 years	5 to 10 years	> than 10 years	Total
	£m	£m	£m	£m	£m
Loans secured by mortgages on immovable property					
Loans to individuals	319.8	937.0	2,962.6	31,163.5	35,382.9
Commercial lending (including SME)	16.6	14.9	62.8	425.4	519.7
Total loans secured on immovable property	**336.4**	**951.9**	**3,025.4**	**31,588.9**	**35,902.6**
Wholesale					
Securitisation positions	-	-	-	3.9	3.9
Central governments or central banks	4,883.8	-	724.3	8,310.1	13,918.2
Covered bonds	-	-	-	-	-
Financial institutions	250.3	224.5	664.8	1,266.5	2,406.1
Multilateral Development Banks	-	-	38.9	-	38.9
Public Sector Entities	-	40.2	40.0	-	80.2
Short-term claims on institutions and corporates	245.1	-	-	-	245.1
Total wholesale exposure	**5,379.2**	**264.7**	**1,468.0**	**9,580.5**	**16,692.4**
Total credit risk exposure (excl. retail and other assets)	**5,715.6**	**1,216.6**	**4,493.4**	**41,169.4**	**52,595.0**

The maturity of exposures is shown on a contractual basis, and it does not take into account any instalments receivable over the life of the exposure.

The risk weighted distribution of exposures on a Group and Solo basis is shown in Table 15 below.

Table 18a - Credit Risk Exposure - Group - 2018

Risk Weight	0%	2%	10%	20%	35%	40%	50%	75%	100%	150%	250%	Deducted	Total	Of which unrated
Exposure Class	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Central governments or central banks	11,902.4	-	-	-	-	-	-	-	-	-	-	-	11,902.4	-
Public sector entities	219.5	-	-	-	-	-	-	-	-	-	-	-	219.5	-
Multilateral development banks	194.8	-	-	-	-	-	-	-	-	-	-	-	194.8	-
Institutions	-	271.8	-	255.5	-	-	639.4	-	-	-	-	-	1,166.7	-
Covered bonds	-	-	309.1	-	-	-	-	-	-	-	-	-	309.1	-
Retail	-	-	-	-	-	-	-	1.1	-	-	-	-	1.1	-
Secured by mortgages on immovable property	-	-	-	-	36,007.4	-	-	353.5	631.5	-	-	-	36,992.4	-
Exposures in default	-	-	-	-	-	-	-	-	136.5	0.4	-	-	136.9	-
Institutions and corporates with a short-term credit assessment	-	-	-	139.8	-	-	-	-	-	-	-	-	139.8	-
Other items*	115.9	-	-	-	-	0.4	-	-	163.0	-	8.3	3.2	290.8	-
Total	**12,432.6**	**271.8**	**309.1**	**395.3**	**36,007.4**	**0.4**	**639.4**	**354.6**	**931.0**	**0.4**	**8.3**	**3.2**	**51,353.5**	**-**

*Other items include securitisation positions and other asset exposure.

Table 18b - Credit Risk Exposure - Group - 2017

Risk Weight	0%	2%	10%	20%	35%	40%	50%	75%	100%	150%	250%	Deducted	Total	Of which unrated
Exposure Class	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Central governments or central banks	13,918.2	-	-	-	-	-	-	-	-	-	-	-	13,918.2	-
Public sector entities	80.2	-	-	-	-	-	-	-	-	-	-	-	80.2	-
Multilateral development banks	38.9	-	-	-	-	-	-	-	-	-	-	-	38.9	-
Institutions	-	234.8	-	1,208.7	-	-	959.2	-	3.4	-	-	-	2,406.1	3.4
Covered bonds	-	-	-	-	-	-	-	-	-	-	-	-	-	-
Retail	-	-	-	-	-	-	-	2.0	-	-	-	-	2.0	-
Secured by mortgages on immovable property	-	-	-	-	34,824.2	-	-	343.3	576.5	-	-	-	35,744.0	-
Exposures in default	-	-	-	-	-	-	-	-	155.8	2.8	-	-	158.6	-
Institutions and corporates with a short-term credit assessment	-	-	-	245.1	-	-	-	-	-	-	-	-	245.1	-
Other items*	127.4	-	-	-	-	-	-	-	166.4	-	12.6	-	306.4	-
Total	**14,164.7**	**234.8**	**-**	**1,453.8**	**34,824.2**	**-**	**959.2**	**345.3**	**902.1**	**2.8**	**12.6**	**-**	**52,899.5**	**3.4**

*Other items include securitisation positions and other asset exposure.

Table 18c - Credit Risk Exposure - Solo - 2018

Risk Weight	0%	2%	10%	20%	35%	40%	50%	75%	100%	150%	250%	Deducted	Total	Of which unrated
Exposure Class	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Central governments or central banks	11,902.4	-	-	-	-	-	-	-	-	-	-	-	11,902.4	-
Public sector entities	219.5	-	-	-	-	-	-	-	-	-	-	-	219.5	-
Multilateral development banks	194.8	-	-	-	-	-	-	-	-	-	-	-	194.8	-
Institutions	-	271.8	-	255.5	-	-	639.4	-	-	-	-	-	1,166.7	-
Covered bonds	-	-	309.1	-	-	-	-	-	-	-	-	-	309.1	-
Retail	-	-	-	-	-	-	-	1.1	-	-	-	-	1.1	-
Secured by mortgages on immovable property	-	-	-	-	36,007.4	-	-	353.5	631.5	-	-	-	36,992.4	-
Exposures in default	-	-	-	-	-	-	-	-	136.5	0.4	-	-	136.9	-
Institutions and corporates with a short-term credit assessment	-	-	-	139.6	-	-	-	-	-	-	-	-	139.6	-
Other items*	2,454.1	-	-	-	-	0.4	-	-	191.9	-	9.9	3.2	2,659.5	-
Total	**14,770.8**	**271.8**	**309.1**	**395.1**	**36,007.4**	**0.4**	**639.4**	**354.6**	**959.9**	**0.4**	**9.9**	**3.2**	**53,722.0**	**-**

*Other items include securitisation positions and other asset exposure.

Table 18d - Credit Risk Exposure - Solo - 2017

Risk Weight	0%	2%	20%	35%	50%	75%	100%	150%	250%	Deducted	Total	Of which unrated
Exposure Class	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	£m
Central governments or central banks	13,918.2	-	-	-	-	-	-	-	-	-	13,918.2	-
Public sector entities	80.2	-	-	-	-	-	-	-	-	-	80.2	-
Multilateral development banks	38.9	-	-	-	-	-	-	-	-	-	38.9	-
Institutions	-	234.8	1,208.7	-	959.2	-	3.4	-	-	-	2,406.1	3.4
Covered bonds	-	-	-	-	-	-	-	-	-	-	-	-
Retail	-	-	-	-	-	2.0	-	-	-	-	2.0	-
Secured by mortgages on immovable property	-	-	-	34,824.2	-	343.3	576.5	-	-	-	35,744.0	-
Exposures in default	-	-	-	-	-	-	155.8	2.8	-	-	158.6	-
Institutions and corporates with a short-term credit assessment	-	-	244.9	-	-	-	-	-	-	-	244.9	-
Other items*	2,730.3	-	-	-	-	-	198.6	-	12.7	-	2,941.6	-
Total	**16,767.6**	**234.8**	**1,453.6**	**34,824.2**	**959.2**	**345.3**	**934.3**	**2.8**	**12.7**	**-**	**55,534.5**	**3.4**

*Other items include securitisation positions and other asset exposure.

For the purposes of generating risk weightings for its wholesale and asset securitisation exposures, the Society uses Fitch and Moody's as External Credit Assessment Institutions (ECAIs), using a composite rating where a counterparty is rated by more than one agency. There has been no change in the Society's use of ECAIs during the year. The following tables show the exposure values associated with each credit quality step for wholesale exposures under the standardised approach:

Table 19a - Sovereign Exposure Credit Quality Steps — 2018
Central Government, Central Banks, MDBs and PSEs

Credit Quality Step	Risk Weight (< 3 months / > 3 months)	Fitch Rating	Moody's Rating	Exposure	Exposure after Mitigation[1]
				£m	£m
1	0%/0%	AAA to AA-	Aaa to Aa3	12,316.7	6,826.6
Total				**12,316.7**	**6,826.6**

Table 19b - Sovereign Exposure Credit Quality Steps — 2017
Central Government, Central Banks, MDBs and PSEs

Credit Quality Step	Risk Weight (< 3 months / > 3 months)	Fitch Rating	Moody's Rating	Exposure	Exposure after Mitigation[1]
				£m	£m
1	0%/0%	AAA to AA-	Aaa to Aa3	14,037.3	8,345.4
Total				**14,037.3**	**8,345.4**

Table 20a - Wholesale Exposure Credit Quality Steps Financial Institutions, Covered Bonds and Short-term claims					2018
Credit Quality Step	Risk Weight (< 3 months / > 3 months)	Fitch Rating	Moody's Rating	Exposure £m	Exposure after Mitigation[1] £m
1	20%/20%	AAA to AA-	Aaa to Aa3	648.7	629.1
2	20%/50%	A+ to A-	A1 to A3	962.8	561.8
3	20%/50%	BBB+ to BBB-	Baa1 to Baa3	4.1	3.4
4	50%/100%	BB+ to BB-	Ba1 to Ba3	-	-
5	50%/100%	B+ to B-	B1 to B3	-	-
6	150%/150%	CCC+ and below	Caa1 and below	-	-
Unrated	100%	Unrated	Unrated	-	-
Total				**1,615.6**	**1,194.3**

Table 20b - Wholesale Exposure Credit Quality Steps Financial Institutions, Covered Bonds and Short-term claims					2017
Credit Quality Step	Risk Weight (< 3 months / > 3 months)	Fitch Rating	Moody's Rating	Exposure £m	Exposure after Mitigation[1] £m
1	20%/20%	AAA to AA-	Aaa to Aa3	1,287.5	328.5
2	20%/50%	A+ to A-	A1 to A3	1,329.8	510.4
3	20%/50%	BBB+ to BBB-	Baa1 to Baa3	30.5	13.6
4	50%/100%	BB+ to BB-	Ba1 to Ba3	-	-
5	50%/100%	B+ to B-	B1 to B3	-	-
6	150%/150%	CCC+ and below	Caa1 and below	-	-
Unrated	100%	Unrated	Unrated	3.4	3.4
Total				**2,651.2**	**855.9**

[1] Mitigation recognises the benefit of collateral held and government guarantees against these investments – see Section 5.6.2 Credit Risk Mitigation: Wholesale

Included within the 2018 exposures above, is approximately £254.3 (31 December 2017: £183.8m) of exposures after mitigation (rated at A+) that relate to centrally cleared counterparties. The exposures have been risk weighted at 2% as per CRD IV rules.

5.3 Securitisation Positions

Issued Securitisations

The Society uses securitisation activities to raise wholesale funding directly and to create collateral which can be used to source additional funding. It has securitised certain mortgage loans by transferring the loans to special purpose entities (SPEs) under the 'Brass' and 'Tombac' securitisation programmes. The SPEs are fully consolidated into the Group accounts.

The transfer of the mortgage loans to the SPEs are not treated as sales by the Society and therefore no gains or losses are recognised, as these structures were not intended to achieve significant transfer of credit risk away from the Society. The Society continues to recognise the mortgage loans on its own balance sheet after the transfer because the risks relating to the underlying mortgage pools, and rewards through the receipt of substantially all of the profits or losses on the securitised loans, remain with the Society and are included in the 'secured by mortgages on immovable property' sections detailed in this document. These assets are held at amortised cost.

There are no specific capital requirements for the securitisation vehicles. As there has not been a transfer of significant credit risk, the Society does not calculate risk weighted asset amounts for any positions it holds in the securitisations and these continue to be calculated in line with capital requirements applied to the underlying mortgage assets. The risks relating to the underlying mortgage pools remain with the Society and are included in the residential mortgage tables detailed throughout this document. Note 35 to the Group Annual Report and Accounts provides more information on the securitisation programme.

The Society has also retained notes from its securitisation issues to be used as collateral for use in sale and repurchase agreements or central bank operations. Investments in self-issued notes and the equivalent 'deemed loan', together with the related income, expenditure and cash-flows are not recognised in the Group's consolidated accounts. This avoids the 'grossing-up' of the financial statements that would otherwise arise. Under the terms of the securitisation programmes, the debt securities in issue are redeemed accordant with the pledged mortgages.

To manage interest rate risk the SPEs enter into derivative transactions. Treatment of derivatives relating to securitisations can be found in Note 34 to the Group Annual Report and Accounts. To manage market and credit risk, the securitisation management group undertakes monthly monitoring of the portfolio, including a review of statistics of the underlying asset pools and compliance with structural tests where applicable using the investor reports published for each of the securities.

The SPEs also represent a liquidity risk to the Society due to legal covenants which need to be fulfilled in the event of a downgrade of the Society. The cash flows resulting from these covenants are in respect of amounts required to collateralise swaps, based on rating agency methodologies. In the event that the Society is downgraded, funds may need to be deposited externally with, or a guarantee obtained from, a suitably rated institution. The cash flows required in the event of downgrade are considered in the Society's ILAAP.

The Society, including any subsidiary, is under no obligation to support any losses that may be incurred by the securitisation programmes or holders of the notes issued, and does not intend to provide such support.

A total of £6.9bn (31 December 2017: £6.5bn) of mortgage loans are currently pledged to the Brass and Tombac securitisation programmes.

For mortgage loans securitised by the Society for the Brass and Tombac programmes as at 31 December 2018, 50 accounts were past due, with a balance of £8.5m. No loss was incurred in the securitisation programmes during the year.

As at 31 December 2018, the nominal value of outstanding debt securities issued through the securitisation programmes was £7.5bn (2017: £7.1bn) of which £6.7bn (2017: £6.4bn) was retained by the Society. The listed notes issued by the securitisation programmes are rated by Moody's and Fitch as Aaa/AAA respectively.

Purchased Securitisations

The Society's exposures listed below relate to purchased securitisation positions, including resecuritisations (which is defined as a securitisation instrument where at least one of the underlying exposures is itself a securitisation).

Table 21 - Securitisation Positions by Investment type	Exposure Values	
	2018	2017
	£m	£m
Combination Note	0.4	3.9
Securities Investment Conduit	3.2	0.0
Total	**3.6**	**3.9**

Securitisation exposures are limited to legacy portfolios which have been in run-off for a significant period and there has been no new investment since 2008. The fair values are based on either quoted market prices, where available, or via valuations provided by external parties.

The Combination Note was subject to further pay downs of principal during the year based on redemptions within the underlying asset pool. The increase in Securities Investment Conduit is due to a write back in the year.

The following table shows the Society's aggregate exposure to purchased securitisations, split by their associated credit quality steps:

Table 22a - Securitised Positions Exposure Credit Quality Steps				2018
Credit Quality Step	Risk Weight	Fitch Rating	Moody's Rating	Exposure £m
1	20%	AAA to AA-	Aaa to Aa3	-
2	50%	A+ to A-	A1 to A3	-
3	100%	BBB+ to BBB-	Baa1 to Baa3	-
4	350%	BB+ to BB-	Ba1 to Ba3	-
5	Deducted	B+ and below	B1 and below	-
Total				**-**

Table 22b - Resecuritised Positions Exposure Credit Quality Steps				2018
Credit Quality Step	Risk Weight	Fitch Rating	Moody's Rating	Exposure £m
1	40%	AAA to AA-	Aaa to Aa3	0.4
2	100%	A+ to A-	A1 to A3	-
3	225%	BBB+ to BBB-	Baa1 to Baa3	-
4	650%	BB+ to BB-	Ba1 to Ba3	-
5	Deducted	B+ and below	B1 and below	3.2
Total				**3.6**

Table 22c - Securitised Positions Exposure Credit Quality Steps				2017
Credit Quality Step	Risk Weight	Fitch Rating	Moody's Rating	Exposure
				£m
1	20%	AAA to AA-	Aaa to Aa3	-
2	50%	A+ to A-	A1 to A3	-
3	100%	BBB+ to BBB-	Baa1 to Baa3	-
4	350%	BB+ to BB-	Ba1 to Ba3	-
5	Deducted	B+ and below	B1 and below	-
Total				-

Table 22d - Resecuritised Positions Exposure Credit Quality Steps				2017
Credit Quality Step	Risk Weight	Fitch Rating	Moody's Rating	Exposure
				£m
1	40%	AAA to AA-	Aaa to Aa3	-
2	100%	A+ to A-	A1 to A3	-
3	225%	BBB+ to BBB-	Baa1 to Baa3	3.9
4	650%	BB+ to BB-	Ba1 to Ba3	-
5	Deducted	B+ and below	B1 and below	-
Total				**3.9**

5.4 Impairment Provisions

5.4.1 Loans Secured by Mortgages on Immovable Property

Further details of the Society's accounting policy for impairment losses on loans and advances to customers is given in Note 1 to the Group Annual Report and Accounts.

The following tables show the balances of loans secured on immovable property, and related impairment provision and fair value credit adjustments, as at 31 December 2018. It should be noted that the figures below show the balances used for provisioning as opposed to capital exposure values (which include potential exposure due to undrawn facilities and pipeline business that do not appear on balance sheet) and therefore do not match the totals in the capital exposure tables in previous sections.

Table 23a - Loans secured on immovable property Individuals	Stage 1	Stage 2	Of which <30 DPD	Of which >30 DPD	Stage 3	Stage 3 POCI	Total
	£m	£m	£m	£m	£m	£m	£m
Customer balance	30,791.6	3,923.5	3,789.0	134.5	345.1	589.8	35,650.0
Impairment provision	1.6	21.5	19.6	1.9	6.6	(1.0)	28.7
Fair value provision	0.1	4.9	4.5	0.4	2.8	29.5	37.3
Carrying value	**30,789.9**	**3,897.1**	**3,764.9**	**132.2**	**335.7**	**561.3**	**35,584.0**
Coverage ratio	**0.0%**	**0.7%**	**0.6%**	**1.8%**	**2.7%**	**4.8%**	**0.2%**

Table 23b - Loans secured on immovable property Commercial	Stage 1	Stage 2	Of which <30 DPD	Of which >30 DPD	Stage 3	Stage 3 POCI	Total
	£m	£m	£m	£m	£m	£m	£m
Customer balance	1,145.8	9.9	3.8	6.1	1.1	26.2	1,183.0
Impairment provision	0.1	0.2	0.2	0.0	0.1	(0.2)	0.2
Fair value provision	-	-	-	-	-	0.6	0.6
Carrying value	**1,145.7**	**9.7**	**3.6**	**6.1**	**1.0**	**25.8**	**1,182.2**
Coverage ratio	**0.0%**	**1.8%**	**4.5%**	**0.1%**	**11.1%**	**1.4%**	**0.1%**

Table 23c - Loans secured on immovable property Total	Stage 1	Stage 2	Of which <30 DPD	Of which >30 DPD	Stage 3	Stage 3 POCI	Total
	£m	£m	£m	£m	£m	£m	£m
Customer balance	31,937.4	3,933.4	3,792.8	140.6	346.2	616.0	36,833.0
Impairment provision	1.7	21.7	19.8	1.9	6.7	(1.2)	28.9
Fair value provision	0.1	4.9	4.5	0.4	2.8	30.1	37.9
Carrying value	**31,935.6**	**3,906.8**	**3,768.5**	**138.3**	**336.7**	**587.1**	**36,766.2**
Coverage ratio	**0.0%**	**0.7%**	**0.6%**	**1.7%**	**2.8%**	**4.7%**	**0.2%**

At each reporting date the Society assesses individual financial assets for impairment. Under IFRS 9, this assessment is based on a forward looking Expected Credit Loss (ECL) approach for financial assets classified at amortised cost and fair value through other comprehensive income, rather than the incurred loss approach applied under IAS 39 until 31 December 2017.

At initial recognition, financial assets are categorised as 'stage 1' and an impairment provision is required for ('ECL') resulting from default events projected within the next 12 months ('12-month ECL'). Subsequently, financial assets are considered to be in 'stage 2' when their credit risk has increased significantly since initial recognition so it is appropriate to recognise lifetime ECL. The Society assesses loans to be in stage 2 when the accounts are more than 30 days past due or there has been a significant relative increase in the lifetime probability of default (PD) compared to initial recognition, and where the PD for retail mortgages is derived based on the customer's credit quality, including analysis of behaviour score and other account characteristics.

The threshold applied to assess whether a significant relative increase has occurred will depend on the credit quality at initial recognition, with a lower percentage change in PD being required for higher risk accounts. For non-retail portfolios, the Society assesses a significant increase in credit risk using a combination of individual and collective information, including monitoring through the watch list process.

Financial assets are included in 'stage 3' when there is objective evidence that the loan is credit impaired, with expected credit losses still calculated on a lifetime basis. The objective evidence that is used to determine whether a loan is impaired is whether they are more than 90 days past due (DPD), have been renegotiated for credit risk reasons, or otherwise considered to be in default (including possession, insolvency and assets beyond term expiry). The assets acquired during the mergers with Chelsea Building Society and N&P Building Society in 2010 and 2011 respectively were subject to adjustments to reflect their 'fair value' at the time of merger rather than the value at which they were initially recorded in Chelsea or N&P's own records. These adjustments included specific adjustments for assets that were credit impaired at the point of acquisition, referred to in the table above as Purchased or Originated Credit Impaired (POCI). To date, cumulative movements have reduced the expected losses on these POCI loans, generating a negative impairment provision under the requirements of IFRS 9.

The Society uses forbearance tools where they are deemed appropriate for an individual customer's circumstances, in line with industry guidance. Forbearance tools, which the Society may offer, include capitalisation, interest only concessions, arrears arrangements, direct debit suspension and term extensions.

Further information on the following areas can be found in the Group Annual Report and Accounts.

Table 24 - For information on:	Refer to:
Impairment Accounting Policy	Note 1
Transitional Adjustments from IAS 39 to IFRS 9	Note 1
Summary of changes in provisions and impact on profit	Note 9
Credit Risk Adjustments and Provisions	Note 39
Geographic distribution of retail mortgage balances	Note 39
Accounts in Forbearance	Note 39

5.4.2 Other

As at 31 December 2018, the Society had an impairment provision of £4.0m on joint venture investments, as shown in Note 41 to the Group Annual Report and Accounts.

5.5 Credit Risk Concentrations

As a UK residential mortgage lender, the Society is inevitably concentrated in this market. Within this overall concentration however, the Society has put in place controls to mitigate undue concentration risk. Further detail of concentrations can be found in Note 39 to the Group Annual Report and Accounts.

5.6 Credit Risk Mitigation

The Society uses a range of techniques to manage the credit risk of its retail, commercial and wholesale lending. The most critical of these is performing an assessment of the ability of a borrower to service the proposed level of borrowing without distress. However, the risk is further mitigated by obtaining collateral for the funds advanced.

5.6.1 Loans Secured by Mortgages on Immovable Property

Loans to Individuals

Residential property is the Society's main source of collateral and means of mitigating credit risk inherent in its residential mortgage portfolios. The initial value of the collateral is established by way of an internal physical inspection of the property and written report by a qualified Royal Institution of Chartered Surveyors (RICS) surveyor. An Automated Valuation Model (AVM) may be used for up to 75% loan to value owner-occupier re-mortgages.

All residential property must be insured to cover property risks, which may be through a third party. Additional protection is also available to borrowers through optional payment protection insurance.

Commercial Lending

The Society also lends to commercial parties through the N&P brand. All commercial loans are secured by a first charge over a commercial or semi-commercial property and are valued by a panel approved valuer. The property must be insured in line with the amount recommended by the valuer. Where the Society lends to a limited company, a guarantee is obtained from the directors of that company.

The Society also lends to housing associations ('Registered Providers'). All of these loans are secured on a portfolio of completed residential properties and are valued by a panel valuer.

5.6.2 Wholesale

Collateral held as security for wholesale assets is determined by the nature of the instrument. Loans, debt securities, and treasury bills are generally unsecured with the exception of securitisation positions and similar instruments, which are secured by pools of financial assets.

The Society's legal documentation with its counterparties for derivative transactions grants legal rights of setoff for those transactions. Accordingly, for credit risk exposures purposes, negative market values on derivatives will offset positive market values on derivatives with the same counterparty in the calculation of credit risk, subject to a minimum absolute exposure of zero by counterparty.

International Swaps and Derivatives Association (ISDA) documentation confers the ability to use designated cash collateral to set against derivative credit risk exposures in the event of a counterparty default. Frequent rebalancing of the collateral requirements reduces the potential increase in future credit risk exposure. For such collateralised exposures, the posting of cash collateral reduces the impact of the current market value to the difference between the market value of the derivatives and the value of the collateral. This difference is limited by the operational use of "thresholds" and "minimum transfer amounts", which set criteria to avoid the movement of small amounts of collateral.

Credit risk is further mitigated by the use of Central Counterparties (CCPs). A CCP is a clearing house that interposes itself between counterparties to contracts traded in one or more financial markets, where a single bilateral contract between the buyer and seller is replaced with two contracts, one between the buyer and CCP and one between the seller and CCP.

Further details on wholesale credit risk can be found in Note 38 to the Group Annual Report and Accounts.

5.7 Counterparty Credit Risk for Derivative Contracts

The Society uses derivative instruments to hedge interest rate risk, foreign currency risk or other factors of a prescribed description arising from fixed rate mortgage lending and savings products, funding and investment activities. Derivatives are only used by the Society in accordance with the Building Societies Act 1997. This means that such instruments are not used in trading activity or for speculative purposes. Counterparty credit risk in the context of this disclosure is the risk that a counterparty to a derivative instrument could default before the final settlement of the transaction's cash flows.

As described in section 5.6.2, risk is mitigated by offsetting the amounts due to the same counterparties ("netting benefits") and by cash deposited by the counterparties ("collateral held"). The following table shows the exposures to counterparty credit risk for derivative contracts as at 31 December 2018. Where derivative transactions meet eligibility for clearing at CCP, counterparty credit risk is replaced by an exposure against the CCP. Counterparty credit risk exposures are calculated using the mark to market method.

Table 25 - Counterparty Credit Risk for Derivative Contracts	2018	2017
	£m	£m
Interest rate contracts	1,575.8	922.4
Foreign exchange contracts	3,583.7	3,092.9
Other contracts	9.6	77.5
Gross positive fair value of contracts	**5,169.1**	**4,092.8**
Netting benefits	(4,485.3)	(3,372.2)
Netted current credit exposure	**683.8**	**720.6**
Collateral held	(216.3)	(298.9)
Net derivatives credit exposure	**467.5**	**421.7**
Add on for potential future exposure	148.6	163.1
Total derivatives exposure	**616.1**	**584.8**

The 'other contracts' element mainly reflects funds provided to counterparties as collateral and the collateral held incorporates the positions that mitigate this exposure.

The net derivatives credit exposure represents the credit exposure to derivative transactions after taking account of legally enforceable netting agreements and collateral arrangements. The total derivatives exposure includes uplifts for potential future exposure under the mark to market method for assessing counterparty credit risk.

If the Society were to be downgraded by a credit ratings agency, there would be no impact on the collateral required to be posted in relation to existing swap agreements, other than those pertaining to securitisations discussed in section 5.3.

Wrong way risk can occur if exposures to a counterparty are negatively correlated to the creditworthiness of that counterparty. As such, there is potential for the exposure to increase as the creditworthiness decreases. Should such a risk arise, this would be taken into account as part of the counterparty review process which allows management to assess what, if any, appropriate mitigating actions are required. Additionally, the Society mitigates wrong way risk by ensuring that exposures on bilateral derivatives are managed via Credit Support Annex (CSA) agreements and margins for centrally cleared swaps which are regularly re-margined.

Internally, capital is allocated to counterparty credit risk based on the methods shown above. Credit limits are determined by internal ratings from credit assessment and approved by ERC.

6 Operational Risk

6.1 Operational Risk Overview

The Society has adopted the standardised approach to all operational risks and has defined operational risk as: "the risk of direct or indirect loss resulting from inadequate or failed internal processes, people, and systems, or from external events".

This means that for the calculation of Pillar 1 capital requirements, the Society calculates its average annual income from prescribed business lines over the past three years. Capital is then held to support operational risk for each business line at prescribed rates from 12% to 18% of its average annual relevant income.

Qualitative requirements for the standardised approach to operational risk have been adopted including:-

- Board and senior management oversight of the Enterprise Risk Management Framework (ERMF). The ERMF is in place to support the implementation of the Enterprise Risk Management Policy which sets out at a high level the requirements for the Society's approach to risk management and outlines the responsibilities for the identification and management of these risks.
- Board approved Group wide ERMF in place with framework components including risk registers, risk assessment, risk response, controls, horizon risks, risk events, Risk & Control Self-Assessment (RCSA), and Second line of defence (2nd LoD) oversight.
- Stress testing and scenario analysis activities undertaken to define the level of capital required to recover from a severe stress scenario event.
- Board, committee and senior management levels reporting on Enterprise and Operational risks with appropriate actions taken as required.

6.2 Enterprise Risk Management Framework (ERMF) and Governance

The Enterprise Risk Management Framework has been created in order to support robust yet efficient risk management which has an important and integral role in the Society:

- Delivering against its Strategy within an appropriate culture;
- Being protected from unplanned financial outcomes;
- Having greater resilience to organisational threats;
- Protecting its customers from unfair outcomes; and
- Demonstrating confidence about itself to external stakeholders.

The Society operates a 'three lines of defence' model towards risk management which seeks to differentiate; those with direct responsibility for the management and control of risk; those with oversight responsibility across the effectiveness and integrity of the enterprise risk management framework; and those providing independent assurance across the first and second lines of defence.

Governance

Oversight and governance arrangements for the setting and management of a robust ERMF are the responsibility of the Board, GRC and ERC. Each committee has a defined Terms of Reference allocating their accountability and responsibilities.

ERC, which is a sub-committee of Group Risk Committee (GRC) from which it has delegated authority, is to ensure the Society's balance between seeking opportunity and managing risk is appropriate:

- Determining and amending the Society's attitude to risk and setting thresholds for endorsement by GRC and Board.
- Ensuring that controls are adequately designed and effective to keep the Society within those thresholds.
- Monitoring and reviewing the risk exposures of the Society in accordance with the Enterprise Risk Management Framework, Risk Appetite, Group Strategy and the Corporate Plan.
- Overseeing that the Society operates compliantly.
- Ensuring clear reporting of risk exposures to GRC and Board

The Society has defined twenty six risk categories (level two), each aligned to one of the four Risk Types (level one). The risk category model currently comprises ten 'Level two' risk categories for Operational Risk, in order to support the consistent description, aggregation, analysis and reporting of operational risks across the Society. A risk and control library has been developed for each category, setting out the 'core' (level three) risks to the Society, together with the associated 'key' controls. The libraries support the creation and maintenance of consistently articulated risk and control registers, whilst providing a framework for lower level risks and controls and supporting the Society's risk and control self-assessment (RCSA) approach. In addition, they enable the alignment and aggregation of risk event data, to validate the self-assessment approach.

6.3 Operational Risk Oversight and Reporting

Oversight (2nd Line of Defence)

Under the 'three lines of defence' model, the second line of defence function is responsible for overseeing the day to day management of risk by (1st Line of Defence). An integrated (2nd Line of Defence) plan for formal oversight reviews is considered and approved by GRC on an annual basis.

Reporting

In order to demonstrate the degree to which risk management has been embedded throughout the organisation, there are a number of reporting mechanisms in place which broadly encompass:

- Current key areas of concern or 'hot topics'.
- The risks with the highest net risk exposure.
- Any key control weaknesses / areas for improvement.
- Significant risk events.
- Any concerns in relation to the funding or progress of mitigating actions.

The first line risk functions are responsible for producing risk reports on a monthly basis in support of Division risk committees / forums, covering the above and any Division specific requirements.

The Enterprise Risk Management team compile risk reporting to support the operation of the Executive (Monthly) and Group (Quarterly) Risk Committees. Again this reporting encompasses the matters highlighted above, together with any specific areas of concern for ERC / GRC attention.

Risk & Control Self-Assessment (RCSA)

The Society operates a RCSA process in order to ensure risks are being effectively controlled both currently and in the future.

The RCSA reports for each business area are aggregated in a Division Summary Report, giving Chief Officers a view of control performance and net risk exposure within their respective areas of responsibility. Risk Category Subject Matter Experts (SMEs) collate the outputs from the Divisional reports relevant to their Risk Category; review these against their

own assurance outcomes, risk events and known areas of concern. They then produce a Category Summary Report which confirms the design effectiveness in relation to each L3 'Key' control and highlights any desirable control enhancements.

The Enterprise Risk Management team summarises the Divisional and Category Summary Reports for ERC and GRC within the Group Risk & Control Assurance Report and provides a 2nd Line opinion of control performance based upon available data, 2nd Line Monitoring and ERM Business Risk Partner opinion.

7 Other Risks

7.1 Interest Rate Risk

Interest rate risk relates to the impact of re-pricing of assets and liabilities through interest rate movements. Details of interest rate risk can be found in Note 36 to the Group's Group Annual Report and Accounts; a description of risk appetite and governance can be found in the Risk Management Report of the Group Annual Report and Accounts.

For assessment of capital requirements, the Society models the impact of a range of severe scenarios on the Society's interest rate position to determine the amount of Pillar 2 capital to hold against this risk.

7.2 Pension Risk

The risk of the Society's defined benefit pension obligations has been modelled, with the help of external actuaries, by applying a severe stress test to the factors that affect the valuation of the scheme. Details of the Society's pension obligations can be found in Note 26 to the Group Annual Report and Accounts.

7.3 Concentration Risk

The Society routinely considers concentrations in products, geographies, channels, income streams and funding sources as part of its strategic planning and has stress tested any such concentrations as part of the ICAAP. A degree of concentration risk is inevitable given the Society's focus in the UK residential mortgage market.

7.4 Business Risk

Consideration is given to the risk that the Society is unable to pursue its short term business plan or longer term strategy. This includes the impact of shifts in the economic, market or regulatory environment that could fundamentally impact on the Society's key Income Statement and Balance Sheet metrics. It can include, for example, the impact of credit ratings downgrades on the Society's ability to raise funding at planned levels and cost.

7.5 Other Risks

After detailed stress testing, no other risks were considered material from a capital perspective as part of the latest ICAAP.

8 Liquidity Management

8.1 Principles

The Society's management of liquidity is based on a number of key principles:

- The Society will at all times maintain liquidity resources which are adequate, both as to amount and quality, to ensure that there is no significant risk that its liabilities cannot be met as they fall due.
- The Society must also ensure that its liquidity resources contain an adequate buffer of high quality, unencumbered assets and it maintains a prudent funding profile.
- The Society must have in place robust strategies, policies, processes and systems that enable it to identify, measure, manage and monitor liquidity risk over a set of time horizons, including intra-day, so as to ensure that it maintains adequate levels of liquidity buffers. These strategies, policies, processes and systems must be tailored to business lines and must include adequate allocation mechanisms of liquidity costs, benefits and risks and ensure that the risks associated with collateral management and asset encumbrance are adequately identified, monitored and managed.
- The Society must adequately stress test their liquidity requirements with contingency funding arrangements in place.

Liquidity risk is monitored on a Group basis with various subsidiaries which could impact the Society's liquidity position (e.g. Accord, securitisation SPVs and the Covered Bond LLP) incorporated into the liquidity risk management process.

The Society employs a number of complimentary indicators within its risk appetite framework, both internal and regulatory, and supplements these with a number of secondary metrics to strengthen the liquidity risk management framework.

Cash flow and liquidity projections are reviewed weekly by the Society and appropriate actions, where required, are taken to adjust the Society's cash flow activity to remain within risk appetite; these meetings also include a discussion of major issues in the wholesale and retail markets, as well as general economic conditions.

GRC is responsible for review and approval of the overall liquidity risk framework, including the Liquidity & Funding Risk Appetite Statement and the Individual Liquidity Adequacy Assessment Process (ILAAP), prior to submission to the Board and regulator (if required).

Liquidity metrics cover the following risks across the Society:

- Pillar 1 risks (i.e. market liquidity and funding liquidity risks). The Liquidity Coverage Ratio (LCR) is a Pillar 1 standard applicable across the European Union which took effect on 1 October 2015. The LCR ensures that a credit institution has an adequate liquidity buffer of unencumbered high-quality liquid assets (HQLA) that can be converted into cash quickly and easily to meet its liquidity needs for a 30 day liquidity stress scenario. The LCR has been designed to make credit institutions less dependent on short-term financing and central bank provision. While the majority of the inflow and outflow weightings are prescribed by the regulator, some outflow weightings are at the discretion of the Society. These are considered as part of the annual ILAAP.
- Pillar 2 risks (i.e. all other material risks not captured by the LCR). The Society captures these risks within its internal liquidity stress test, the Overall Liquidity Requirements (OLR) test. The construction and assumptions in this test are outlined and agreed in the ILAAP.

8.2 Internal Liquidity Adequacy Assessment Process (ILAAP)

The Society undertakes at least annually an ILAAP, which is an internal assessment of its liquidity risk requirement.

This process includes:

- Identification of the relevant liquidity risk drivers for the Society;
- Development of severe but plausible liquidity risk scenarios to enable an assessment of the requirement of the Society to be established. These scenarios are approved by both the ERC and GRC prior to any development work being undertaken on the impacts of the scenarios;
- Relevant business areas are then responsible for determining the way in which each of the scenarios would impact on the relevant elements of the balance sheet;
- All the relevant assessments are then consolidated to determine which of the scenarios generate the worst case outcome. This is documented in the ILAAP and will, once approved, form part of the daily stress testing process;
- The ILAAP is then reviewed by the second line Prudential Risk team before being submitted to GRC and ultimately the Board for approval.

8.3 Liquidity Coverage Ratio (LCR)

The following table shows the breakdown of the components of the LCR on both a consolidated and solo basis and states the values for each of the four calendar quarters (January – March, April – June, July – September, October – December). The values have been calculated as the simple averages of month-end observations over the twelve months preceding the end of each quarter.

Table 26a - Breakdown of components of the LCR - Consolidated

Quarter ending	31 March 2018	30 June 2018	30 September 2018	31 December 2018
Number of data points used in the calculation of averages	12	12	12	12
	£m	£m	£m	£m
Liquidity Buffer	4,405	4,416	4,462	4,598
Total Net Cash Outflows	2,672	2,706	2,766	2,838
Liquidity Coverage Ratio (%)	165.3%	163.7%	162.1%	162.9%

Table 26b - Breakdown of components of the LCR - Solo

Quarter ending	31 March 2018	30 June 2018	30 September 2018	31 December 2018
Number of data points used in the calculation of averages	12	12	12	12
	£m	£m	£m	£m
Liquidity Buffer	4,405	4,416	4,462	4,598
Total Net Cash Outflows	2,625	2,660	2,713	2,783
Liquidity Coverage Ratio (%)	168.2%	166.5%	165.2%	166.1%

8.3.1 Liquidity Buffer

The liquidity buffer includes assets with the potential to be converted quickly and easily into cash if a stress were to materialise. There are three categories of liquidity buffer with differing levels of perceived quality: Level 1 (highest quality and perceived to be the most liquid of assets), Level 2A (lower quality) and Level 2B (lowest quality and perceived to be the least liquid of the assets eligible for inclusion in the liquidity buffer). Assets included in the liquidity buffer must be unencumbered, capable of being valued easily and either listed on a recognised exchange or tradable via outright sale or via repurchase transactions. The asset classes are also subject to minimum requirements to determine their 'Level' i.e. how easily they could be converted into cash in a stress.

The liquidity buffer must comply with the following requirements:

- Minimum of 60% of the buffer must be composed of Level 1 assets;
- Minimum of 30% of the buffer must be composed of Level 1 assets excluding extremely high quality covered bonds;
- A maximum of 15% of the buffer may be held in Level 2B assets.

8.3.1.1 Level 1 Assets

Level 1 assets include coins and banknotes, exposures to central banks, assets representing claims on or guaranteed by central or regional governments, local authorities or public sector entities, exposures in the form of extremely high quality covered bonds and assets representing claims on or guaranteed by multilateral development banks.

All Level 1 eligible assets can be held at full value within the LCR, apart from extremely high quality covered bonds which are subject to a haircut of at least 7%. As at 31 December 2018, all of the Society's assets within the liquid buffer were designated as Level 1.

8.3.1.2 Level 2A Assets

Level 2A assets include assets representing claims on or guaranteed by central or regional governments, local authorities or public sector entities, exposures in the form of high quality covered bonds and corporate debt securities. All Level 2A eligible assets are subject to a haircut of at least 15%. As at 31 December 2018 the Society held no Level 2A eligible assets.

8.3.1.3 Level 2B Assets

Level 2B assets comprise of asset-backed securities, corporate debt securities, shares, restricted-use committed facilities provided by a central bank and exposures in the form of high quality covered bonds. All Level 2B eligible assets are subject to a haircut of at least 25%. As at 31 December 2018 the Society held no Level 2B eligible assets.

8.3.2 Total Net Cash Outflows

Net cash outflows is defined as the total expected cash outflows, minus total expected cash inflows, for the subsequent 30 days. Total expected cash outflows are calculated by multiplying the outstanding balances of various types of liabilities and off-balance sheet commitments by the stress rates at which they are expected to run off or be drawn down. Total expected cash inflows are calculated by multiplying the outstanding balances of various categories or contractual receivables by the rates at which they are expected to flow in. Total cash inflows are subject to an aggregate cap of 75% of total expected cash outflows, thereby ensuring a minimum amount of liquid buffer at all times.

The primary driver of outflows in the LCR stems from the Society's retail savings book. Other areas of the business that generate outflows include the wholesale funding book, mortgage pipeline and operational expenses. The main drivers of inflows in the LCR come from the Society's mortgage book via contractual repayments. Other areas of the business that

contribute inflows include the Society's commercial lending as well as coupons from both the retained wholesale funding book and the assets included within the liquidity buffer.

9 Remuneration

The table below shows the remuneration awarded to senior management and other material risk takers during the financial year.

Table 27a - Remuneration awarded during the financial year ended 31 December 2018			
	Senior Management	Other material risk takers	Total
	£m	£m	£m
Fixed remuneration	6.6	0.5	7.1
Variable remuneration	1.9	0.0	1.9
Total remuneration	**8.5**	**0.6**	**9.0**

Table 27b - Remuneration awarded during the financial year ended 31 December 2017			
	Senior Management	Other material risk takers	Total
	£m	£m	£m
Fixed remuneration	8.4	0.9	9.3
Variable remuneration	2.9	0.1	3.0
Total remuneration	11.3	1.0	12.3

Further disclosures on remuneration are contained in various sections of the Group Annual Report and Accounts.

The Society's Reward policy can be found on the Society's website:

https://www.ybs.co.uk/your-society/inside-your-society/corporate-governance/committees.html

10 Appendix

10.1 Appendix 1 - Asset Encumbrance

The amounts disclosed in Templates A and C below are median values calculated using quarterly data and have been prepared in accordance to EBA Guideline EBA/GL/2014/03 on the disclosure of encumbered and unencumbered assets and as such differ from the disclosures contained in the Group Annual Report and Accounts.

Template A: Assets

Table 28a - Encumbered Assets (Template A)				2018
	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
	£m	£m	£m	£m
Assets of the reporting institution	10,122.3		31,560.6	
of which:				
Equity instruments				
Debt securities	457.5	457.5	1,172.7	1,172.7
Other assets			908.5	

Table 28b - Encumbered Assets (Template A)				2017
	Carrying amount of encumbered assets	Fair value of encumbered assets	Carrying amount of unencumbered assets	Fair value of unencumbered assets
	£m	£m	£m	£m
Assets of the reporting institution	8,610.9		30,687.9	
of which:				
Equity instruments				
Debt securities	81.9	81.9	446.0	446.0
Other assets			835.2	

Template B: Collateral

In accordance with PRA Supervisory Statement ‘CRD IV: compliance with the European Banking Authority’s Guidelines on the disclosure of encumbered and unencumbered assets’ (SS11/14), the Society has elected to apply the waiver regarding disclosure of collateral received, therefore Template B has not been disclosed.

Template C: Encumbered Assets/ Collateral Received and Associated Liabilities

Table 29 - Encumbered Assets/Collateral Received and Associated Liabilities (Template C)				
	Matching liabilities, contingent liabilities or securities lent		Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered	
	2018	2017	2018	2017
	£m	£m	£m	£m
Carrying amount of selected financial liabilities	6,492.7	5,010.8	4,737.2	5,996.8

Template D: Information on importance of encumbrance

Encumbrance occurs through the pledging of assets to secured creditors; such assets become unavailable for other purposes. The most material sources of encumbrance for the Society is secured funding via the Society's covered bond and securitisation programmes which are supported by pledging mortgage assets as collateral. Assets are encumbered in accordance with the contractual requirements of these programmes. Further detail on these activities is set out in Note 35 to the Group Annual Report and Accounts. These programmes are continually assessed and a prudent buffer of over-collateralisation is voluntarily maintained for operational efficiency.

The Society also pledges debt securities as collateral in sale and repurchase transactions. An additional source of encumbrance is the collateralisation of derivative liabilities. The Society treats some cash and balances with the Bank of England, 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 Society's covered bond and securitisation programmes; as these are not available for use in the Society's day-to-day operations.

10.2 Appendix 2 – Own Funds Disclosure Template

The table below contains the own funds of the Capital Group and Solo-consolidated Group on a transitional and end-point basis and have been prepared in accordance with Regulation (EU) 1423/2013, blank cells have been removed from the template.

Table 30a - Own funds disclosure template - Group		Transitional		End-Point	
		2018	2017	2018	2017
		£m	£m	£m	£m
Common Equity Tier 1 (CET1) Capital: instruments and reserves					
2	Retained earnings	2,377.2	2,215.4	2,377.2	2,215.4
3	Accumulated other comprehensive income (and other reserves)	(4.1)	44.5	(4.1)	44.5
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	149.8	124.5	149.8	124.5
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	2,522.9	2,384.4	2,522.9	2,384.4
Common Equity Tier 1 (CET1) capital: regulatory adjustments					
7	Additional value adjustments (negative amount)	(2.3)	(1.6)	(2.3)	(1.6)
8	Intangible assets (net of related deferred tax liability (negative amount)	(39.8)	(31.3)	(39.8)	(31.3)
11	Fair value reserves related to gains or losses on cash flow hedges	1.8	3.6	1.8	3.6
12a	IFRS 9 transitional arrangements	0.4	-	0.4	-
15	Defined-benefit pension fund assets (negative amount)	(56.9)	(71.4)	(56.9)	(71.4)
20a	Exposure amount of the following items which qualify for a RW of 1,250%, where the institution opts for the deduction alternative	(3.2)	-	(3.2)	-
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	(100.0)	(100.7)	(100.0)	(100.7)
29	Common Equity Tier 1 (CET1) capital	2,422.9	2,283.7	2,422.9	2,283.7
Additional Tier 1 (AT1) capital: instruments					
33	Amount of qualifying items referred to in Article 484 (4) and the related share premium accounts subject to phase out from AT1	2.5	3.2	-	-
36	Additional Tier 1 (AT1) capital before regulatory adjustments	2.5	3.2	-	-
Additional Tier 1 (AT1) capital: regulatory adjustments					
43	Total regulatory adjustments to Additional Tier 1 (AT1) capital	-	-	-	-
44	Additional Tier 1 (AT1) capital	2.5	3.2	-	-
45	Tier 1 capital (T1 = CET1 + AT1)	2,425.4	2,286.9	2,422.9	2,283.7
Tier 2 (T2) capital: instruments and provisions					

Table 30a - Own funds disclosure template - Group (Continued)		Transitional		End-Point	
		2018	2017	2018	2017
		£m	£m	£m	£m
46	Capital instruments and the related share premium accounts	585.1	589.2	585.1	589.2
50	Credit risk adjustments	-	24.5	-	24.5
51	Tier 2 (T2) capital before regulatory adjustments	585.1	613.7	585.1	613.7
Tier 2 (T2) capital: regulatory adjustments					
57	**Total regulatory adjustments to Tier 2 (T2) capital**	-	-	-	-
58	**Tier 2 (T2) capital**	585.1	613.7	585.1	613.7
59	Total capital (TC = T1 + T2)	3,010.5	2,900.6	3,008.0	2,897.4
60	Total risk weighted assets	14,841.3	14,449.4	14,841.3	14,449.4
Capital ratios and buffers					
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	16.3%	15.8%	16.3%	15.8%
62	Tier 1 (as a percentage of total risk exposure amount)	16.3%	15.8%	16.3%	15.8%
63	Total capital (as a percentage of total risk exposure amount)	20.3%	20.1%	20.3%	20.1%
64	Institution specific buffer requirement (CET1 requirement in accordance with Article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)	2.9%	1.3%	2.9%	1.3%
65	of which: capital conservation buffer requirement	1.9%	1.3%	1.9%	1.3%
66	of which: countercyclical buffer requirement	1.0%	-	1.0%	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	9.9%	8.1%	9.9%	8.1%
Applicable caps on the inclusion of provisions in Tier 2					
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	-	24.5	-	24.5
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	185.5	180.6	185.5	180.6
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)					
82	Current cap on AT1 instruments subject to phase out arrangements	2.5	3.2	-	-
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	3.6	3.2	-	-

Table 30b - Own funds disclosure template - Solo		Transitional		End-Point	
		2018	2017	2018	2017
		£m	£m	£m	£m
Common Equity Tier 1 (CET1) Capital: instruments and reserves					
2	Retained earnings	2,361.5	2,210.6	2,361.5	2,210.6
3	Accumulated other comprehensive income (and other reserves)	(4.2)	43.5	(4.2)	43.5
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	125.8	114.6	125.8	114.6
6	Common Equity Tier 1 (CET1) capital before regulatory adjustments	2,483.1	2,368.7	2,483.1	2,368.7
Common Equity Tier 1 (CET1) capital: regulatory adjustments					
7	Additional value adjustments (negative amount)	(2.1)	(1.3)	(2.1)	(1.3)
8	Intangible assets (net of related deferred tax liability (negative amount)	(39.8)	(31.3)	(39.8)	(31.3)
11	Fair value reserves related to gains or losses on cash flow hedges	1.8	3.6	1.8	3.6
12a	IFRS 9 transitional arrangements	0.4	-	0.4	-
15	Defined-benefit pension fund assets (negative amount)	(56.9)	(71.4)	(56.9)	(71.4)
20a	Exposure amount of the following items which qualify for a RW of 1250%, where the institution opts for the deduction alternative	(3.2)	-	(3.2)	-
28	Total regulatory adjustments to Common Equity Tier 1 (CET1)	(99.8)	(100.4)	(99.8)	(100.4)
29	Common Equity Tier 1 (CET1) capital	2,383.3	2,268.3	2,383.3	2,268.3
Additional Tier 1 (AT1) capital: instruments					
33	Amount of qualifying items referred to in Article 484 (4) and the related share premium accounts subject to phase out from AT1	2.5	3.2	-	-
36	Additional Tier 1 (AT1) capital before regulatory adjustments	2.5	3.2	-	-
Additional Tier 1 (AT1) capital: regulatory adjustments					
43	Total regulatory adjustments to Additional Tier 1 (AT1) capital	-	-	-	-
44	Additional Tier 1 (AT1) capital	2.5	3.2	-	-
45	Tier 1 capital (T1 = CET1 + AT1)	2,385.8	2,271.5	2,383.3	2,268.3
Tier 2 (T2) capital: instruments and provisions					
46	Capital instruments and the related share premium accounts	585.1	589.2	585.1	589.2
50	Credit risk adjustments	-	24.5	-	24.5
51	Tier 2 (T2) capital before regulatory adjustments	585.1	613.7	585.1	613.7
Tier 2 (T2) capital: regulatory adjustments					
57	**Total regulatory adjustments to Tier 2 (T2) capital**	-	-	-	-

Table 30b - Own funds disclosure template - Solo (Continued)		Transitional		End-Point	
		2018	2017	2018	2017
		£m	£m	£m	£m
58	**Tier 2 (T2) capital**	585.1	613.7	585.1	613.7
59	Total capital (TC = T1 + T2)	2,970.9	2,885.2	2,968.4	2,882.0
60	Total risk weighted assets	14,855.2	14,489.8	14,855.2	14,489.8
Capital ratios and buffers					
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	16.0%	15.7%	16.0%	15.7%
62	Tier 1 (as a percentage of total risk exposure amount)	16.1%	15.7%	16.0%	15.7%
63	Total capital (as a percentage of total risk exposure amount)	20.0%	19.9%	20.0%	19.9%
64	Institution specific buffer requirement (CET1 requirement in accordance with Article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)	2.9%	1.3%	2.9%	1.3%
65	of which: capital conservation buffer requirement	1.9%	1.3%	1.9%	1.3%
66	of which: countercyclical buffer requirement	1.0%	-	1.0%	-
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	9.6%	8.0%	9.6%	8.0%
Applicable caps on the inclusion of provisions in Tier 2					
76	Credit risk adjustments included in T2 in respect of exposures subject to standardised approach (prior to the application of the cap)	-	24.5	-	24.5
77	Cap on inclusion of credit risk adjustments in T2 under standardised approach	185.7	181.1	185.7	181.1
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)					
82	Current cap on AT1 instruments subject to phase out arrangements	2.5	3.2	-	-
83	Amount excluded from AT1 due to cap (excess over cap after redemptions and maturities)	3.6	3.2	-	-

10.3 Appendix 3 – Capital Instruments Main Features Template

The table below contains the capital instruments of the Society and has been prepared in accordance with Commission Implementing Regulation (EU) 1423/2013.

Table 31 - Capital Instruments Main Features						
1	Issuer	Yorkshire Building Society	Yorkshire Building Society	Yorkshire Building Society	Yorkshire Building Society	Yorkshire Building Society
2	Unique Identifier	XS1140677250	XS0096893465	XS0498549194	XS1681849300	XS0247065674
3	Governing law(s) of the instrument	English	English	English	English	English
Regulatory treatment						
4	Transitional CRR rules	Tier 2	Tier 2	Tier 2	Tier 2	Additional Tier 1
5	Post-transitional CRR rules	Tier 2	Tier 2	Tier 2	Tier 2	Ineligible
6	Eligible at solo/(sub-)consolidated / solo & (sub-)consolidated	Solo and Consolidated	Solo and Consolidated	Solo and Consolidated	Solo and Consolidated	Solo and Consolidated
7	Instrument type (types to be specified by each jurisdiction)	Tier 2	Tier 2	Tier 2	Tier 2	PIBS
8	Amount recognised in regulatory capital (currency in million, as of most recent reporting date)	£248,729,133	£3,983,124	£26,868,691	£305,513,944	£2,456,450
9	Nominal amount of instrument	£250,000,000	£3,900,000	£25,605,500	£300,000,000	£6,056,000
9a	Issue price	99.267	97.983	100	99.389	100
9b	Redemption price	100	100	100	100	100
10	Accounting classification	Liability-amortised cost	Liability-amortised cost	Liability-amortised cost	Liability-amortised cost	Liability-amortised cost
11	Original date of issuance	20/11/2014	26/04/1999	01/04/2010	13/09/2017	27/03/2006
12	Perpetual or dated	Dated	Dated	Dated	Dated	Perpetual
13	Original maturity date	20/11/2024	26/04/2024	01/04/2025	13/09/2028	Perpetual
14	Issuer call subject to prior supervisory approval	Yes	n/a	n/a	Yes	n/a
15	Optional call date, contingent call dates and redemption amount	20/11/2019	n/a	n/a	13/09/2027	27/03/2019
16	Subsequent call dates, if applicable	n/a	n/a	n/a	n/a	Quarterly
Coupon / dividends						
17	Fixed or floating dividend/coupon	Fixed	Fixed	Fixed	Fixed	Fixed
18	Coupon rate and any related index	4.125	6.375	13.500	3.375	5.649
19	Existence of a dividend stopper	n/a	n/a	n/a	n/a	n/a
20a	Fully discretionary, partially discretionary or mandatory (in terms of timing)	n/a	n/a	n/a	n/a	Fully
20b	Fully discretionary, partially discretionary or mandatory (in terms of timing)	n/a	n/a	n/a	n/a	Fully
21	Existence of step up or other incentive to redeem	No	No	No	No	No
22	Non-cumulative or cumulative	n/a	n/a	n/a	n/a	n/a

Table 31 - Capital Instruments Main Features - Continued						
23	Convertible or non-convertible	Non-convertible	Non-convertible	Convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	n/a	n/a	CET < 5% contractual approach	n/a	n/a
25	If convertible, fully or partially	n/a	n/a	Fully	n/a	n/a
26	If convertible, conversion rate	n/a	n/a	100	n/a	n/a
27	If convertible, mandatory or optional conversion	n/a	n/a	Mandatory	n/a	n/a
28	If convertible, specify instrument type convertible into	n/a	n/a	Profit Participating Deferred Shares (PPDS)	n/a	n/a
29	If convertible, specify issuer of instrument it converts into	n/a	n/a	Yorkshire Building Society	n/a	n/a
30	Write-down features	n/a	n/a	n/a	n/a	n/a
31	If write-down, write-down trigger(s)	n/a	n/a	n/a	n/a	n/a
32	If write-down, full or partial	n/a	n/a	n/a	n/a	n/a
33	If write-down, permanent or temporary	n/a	n/a	n/a	n/a	n/a
34	If temporary write-down, description of write-up mechanism	n/a	n/a	n/a	n/a	n/a
35	Position in subordination hierarchy in liquidation (specify instrument type immediately senior to instrument)	Senior unsecured	Senior unsecured	Senior unsecured	Senior unsecured	Tier 2
36	Non-compliant transitioned features	No	No	No	No	No
37	If yes, specify non-compliant features	n/a	n/a	n/a	n/a	n/a

10.4 Appendix 4 - Leverage Disclosure Template

The table below contains the CRR leverage ratio disclosure and has been prepared in accordance with Commission implementing Regulation (EU) 2016/200; blank cells have been removed from the template.

Reference date	31 December 2018 (31 December 2017 for comparatives)
Entity name	Yorkshire Building Society
Level of application	Consolidated

Table 32 - LRSum: Summary reconciliation of accounting assets and leverage ratio exposures		2018 £m	2017 £m
1	Total assets as per published financial statements	43,049.2	42,041.7
4	Adjustments for derivative financial instruments	(144.2)	(151.3)
6	Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	2,393.7	3,338.7
7	Other adjustments	(100.0)	(104.3)
8	**Leverage ratio total exposure measure**	**45,198.7**	**45,124.8**

Table 33 - LRCom: Leverage ratio common disclosure		2018 £m	2017 £m
On-balance sheet exposures (excluding derivatives and SFTs)			
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	42,484.8	41,449.9
2	(Asset amounts deducted in determining Tier 1 capital)	(100.0)	(104.3)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets)**	**42,384.8**	**41,345.6**
Derivative exposures			
4	Replacement cost associated with all derivatives transactions (i.e. net of eligible cash variation margin)	479.3	508.6
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	148.6	163.1
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	(207.8)	(231.2)
11	Total derivatives exposures	**420.1**	**440.5**
Other off-balance sheet exposures			
17	Off-balance sheet exposures at gross notional amount	3,856.4	4,196.2
18	(Adjustments for conversion to credit equivalent amounts)	(1,462.7)	(857.5)
19	**Other off-balance sheet exposures**	**2,393.7**	**3,338.7**
Capital and total exposure measure			
20	**Tier 1 capital**	**2,425.4**	**2,286.9**
21	**Leverage ratio total exposure measure**	**45,198.6**	**45,124.8**
Leverage Ratios			
22	Leverage ratio	5.4%	5.1%
Choice on transitional arrangements and amount of derecognised fiduciary items			
EU-23	Choice on transitional arrangements for the definition of the capital measure	Transitional	Transitional

Table 34 - Table LRSpl: Split-up of on balance sheet exposures (excluding derivatives, SFTs and exempted exposures)		2018 £m	2017 £m
EU-1	Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	42,484.8	41,449.9
EU-3	Banking book exposures, of which:	42,484.8	41,449.9
EU-4	Covered bonds	309.1	-
EU-5	Exposures treated as sovereigns	4,764.2	5,727.3
EU-7	Institutions	123.5	170.2
EU-8	Secured by mortgages of immovable properties	36,643.1	35,024.4
EU-11	Exposures in default	127.5	149.4
EU-12	Other exposures (e.g. equity, securitisations, and other non-credit obligation assets)	517.4	378.6

Table 35 - LRQua - Qualitative information on managing the risk of excessive leverage and the factors impacting on the leverage ratio	
1	Description of the processes used to manage the risk of excessive leverage
	The Society has a CRR leverage ratio of 5.4%, and a UK leverage ratio of 5.8%. The Leverage ratio is a key risk indicator for the Society and is monitored by the Board quarterly, with the Society producing a strategic reassessment of its leverage risk appetite annually. The Society produces a five year capital plan of the leverage ratio annually, reforecasting this position more frequently during the year.
2	Description of the factors that had an impact on the leverage Ratio during the period to which the disclosed leverage Ratio refers.
	The key factors impacting the Society's CRR leverage ratio during the period are primarily an increase in Tier 1 capital due to increased general reserves offset by increased leverage exposure due to an increase in balance sheet assets.

10.5 Appendix 5 – Countercyclical Capital Buffer

The table below contains the Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer and has been prepared in accordance with Commission Delegated Regulation (EU) 2015/1555.

In accordance with Commission Delegated Regulation (EU) 1152/2014, due to foreign exposures not exceeding 2% of the Society's aggregate exposures, all exposures have been allocated to the UK. For the purposes of this calculation this includes loans secured by mortgages on immoveable property, retail, securitisation positions and other assets. The Society has no trading book exposures.

Table 36a - Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer 2018

	£m		£m		£m				%	%
Breakdown by country	General Credit Exposures		Securitisation exposure		Own funds requirements				Own funds requirement weights	Countercyclical capital buffer rate
	Exposure value for SA	Exposure value for IRB	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total		
UK	37,417.7	-	3.5	-	1,095.3	-	-	1,095.3	100.0%	1.0%

Table 36b - Geographical distribution of credit exposures relevant for the calculation of the countercyclical capital buffer 2017

	£m		£m		£m				%	%
Breakdown by country	General Credit Exposures		Securitisation exposure		Own funds requirements				Own funds requirement weights	Countercyclical capital buffer rate
	Exposure value for SA	Exposure value for IRB	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total		
UK	36,207.1	-	3.9	-	1,060.6	-	0.7	1,061.3	100.0%	-

The table below contains the Society's specific countercyclical buffer rate.

Table 37 - Amount of institution-specific countercyclical capital buffer	2018	2017
	£m	£m
Total risk exposure amount*	14,841.3	14,449.4
Institution specific countercyclical buffer rate	1.0%	0.0%
Institution specific countercyclical buffer requirement	148.4	0.0

* The total risk exposure amount provided is equal to total RWAs.

Glossary

Term	Definition
Additional Tier 1 (AT1)	Any remaining eligible Permanent Interest Bearing Shares (PIBS).
Arrears	A customer is defined as being in arrears when they fall behind in meeting their obligations to pay their mortgage and as a result there is an outstanding loan commitment that is overdue.
Average Risk Weight (RW)	Risk weighted assets divided by capital exposure.
Behaviour score	Behavioural scoring is used throughout the life of a customer relationship to inform management strategies for each customer.
Common Equity Tier 1 (CET1) capital	The highest quality regulatory capital resources, comprising retained earnings less regulatory adjustments, as defined under CRD IV. Equivalent to Core Tier 1 defined under previous CRD legislation.
Common Equity Tier 1 capital ratio	The ratio of Common Equity Tier 1 Capital to Risk Weighted Assets.
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.
Credit Quality Steps (CQS)	A credit quality assessment scale as set out in CRD IV.
CRD IV	A package of legislation incorporating a Regulation (CRR) and a Directive (CRD) that implements the Basel III framework in Europe.
Credit risk	The risk of financial loss arising from a failure of a customer or counterparty to settle their financial and contractual obligations as they fall due.
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.
Credit Valuation Adjustment (CVA)	These are adjustments applied to the fair values of derivatives to reflect the creditworthiness of the counterparty.
External Credit Assessment Institution (ECAI)	An ECAI (e.g. Moody's, Standard and Poor's, Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
EEA parent institution	A parent financial institution situated in a Member State of the European Economic Area which is not a subsidiary of another financial institution also situated in the EEA.
Financial Conduct Authority (FCA)	The UK conduct regulator which is responsible for regulation of conduct in retail, as well as wholesale, financial markets and the infrastructure that supports those markets. The FCA's objective is to protect consumers, promote competition and enhance market integrity.
Guarantee	An agreement by a third party to cover the potential loss to a credit institution should a specified counterparty default on their obligations.
International Financial Reporting Standard 9 (IFRS 9)	The IFRS 9 accounting standard sets out the requirements for the classification and measurement of financial assets, financial liabilities and some contracts to buy or sell non-financial items. It includes requirements on impairment and hedge accounting.
Individual Capital Assessment (ICA)	The document produced as a result of the ICAAP.

Internal Capital Adequacy Assessment Process (ICAAP)	The Society's internal assessment of the levels of capital that need to be held by the Society to meet its regulatory capital requirements.
Individual Capital Guidance (ICG)	The minimum amount of capital the Society should hold as set by the PRA under Pillar 2.
Individual Liquidity Adequacy Assessment (ILAA)	The Society's internal assessment of the levels of liquidity that need to be held by the Society to meet its regulatory liquidity requirements.
Interest rate risk	Interest rate risk is the exposure of a firm's financial condition to adverse movements in interest rates.
Impaired loans	Loans where there is evidence to suggest a measurable decrease in the present value of cash flows expected which has occurred after initial recognition of the asset, but before the statement of financial position date.
Individually impaired loans	Where retail or commercial mortgages are in arrears by three months or more, they are individually assessed for impairment. Commercial loans less than three months in arrears are also individually impaired where other factors suggest a measurable decrease in the present value of their future cash flows.
Internal Ratings Based (IRB)	Approach to calculating capital requirements where lenders use their own models of risk to determine the appropriate minimum capital requirement.
International Swaps and Derivatives Association (ISDA)	The global trade association for over-the-counter (OTC) derivatives, and providers of the industry-standard ISDA documentation.
Loan-to-value ratio (LTV)	A ratio showing outstanding loan balance as a percentage of the value of the security.
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.
Minimum Capital Requirement	The minimum amount of regulatory capital that a financial institution must hold to meet the Pillar 1 requirements for credit, operational risk and market risk.
Minimum Requirement of Eligible Liabilities (MREL)	The minimum requirements a financial institution must hold to meet the loss absorption and recapitalisation components if an institution were to fail.
Netting	The ability to reduce credit risk exposures by offsetting the value of any deposits against loans to the same counterparty.
Operational risk	The risk of direct and indirect loss resulting from inadequate or failed internal processes, people and systems or from external events.
Past due	Loans which are in arrears by 3 months or more.
Permanent Interest Bearing Shares (PIBS)	Unsecured, sterling denominated Tier 1 capital instruments repayable at the option of the Society.
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) – ICG is an outcome from Pillar 2.
Pillar 3	The part of the Basel III Framework which sets out the disclosure requirements for firms to publish details of their risks, capital and risk management. The aims are greater transparency and strengthening market discipline.

Provisions	Amounts set aside to cover incurred losses associated with credit risks.
Prudential Regulation Authority (PRA)	The UK prudential regulator, which is a part of the Bank of England and alongside the FCA, has responsibility for the oversight of building societies, banks and insurers. The PRA's objective is to promote the safety and soundness of regulated firms.
Prudent Valuation Adjustment (PVA)	A regulatory deduction applied to CRD IV Common Equity Tier 1 capital calculated in accordance with Article 105 of the Capital Requirements Regulation (CRR). The purpose of the Prudent Valuation Adjustment is to ensure that the valuation of financial instruments for capital reporting is at the more conservative end of any range of plausible valuations.
Resecuritisation	A securitisation transaction or scheme that includes at least one securitisation within its underlying asset pool.
Risk Weighted Assets (RWA)	A regulatory measure that adjusts the value of assets to reflect their level of risk when calculating capital requirements.
Securitisation	A transaction or scheme where assets are sold to a Special Purpose Vehicle (SPV) in return for immediate cash payment. That vehicle raises the immediate cash payment by issuing debt securities in the form of tradable 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. Securitisations may be purchased or retained.
SME	Small and medium-sized enterprise.
SREP	Supervisory Review and Evaluation Process, the PRA assessment of a firm's own capital assessment (ICA) under Basel III Pillar 2.
Stress testing	Various techniques that are used to gauge the potential vulnerability to exceptional but plausible events.
Subordinated debt	Tier 2 capital that is subordinated to the claims of all depositors, creditors and members holding shares in the Society (other than holders of PIBS).
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 between 12-18%, depending on the underlying business being considered.
Tier 1 (T1) capital	The sum total of Common Equity Tier 1 and Additional Tier 1 capital.
Tier 1 capital ratio	The ratio of Tier 1 capital to Risk Weighted Assets.
Tier 2 (T2) capital	A measure of regulatory capital that includes subordinated liabilities and provisions for collective impairment, less regulatory adjustments.
Total capital ratio	The ratio of total capital to Risk Weighted Assets.
Total Capital Requirement (TCR)	The total of Pillar 1 requirements and Pillar 2A requirements

References to 'YBS Group' or 'Yorkshire Group' refer to Yorkshire Building Society, the trading names under which it operates (Chelsea Building Society, the Chelsea, Norwich & Peterborough Building Society, N&P and Egg) and its subsidiary companies. Yorkshire Building Society is a member of the Building Societies Association and is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority and the Prudential Regulation Authority. Yorkshire Building Society is entered in the Financial Services Register and its registration number is 106085. Head Office: Yorkshire House, Yorkshire Drive, Bradford BD5 8LJ. **ybs.co.uk**

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