
# ANNUAL REPORT AND ACCOUNTS | 2014

*Always there for our Members. Since 1849*

Saffron Building Society

Members' Event June 2014

# OUR VALUES

We believe it's our traditions and roots that make a real difference for our Members.

**Genuine**
Our business is built on two things – trust and serving our Members, not shareholders.

**Approachable**
We are friendly and proud of our place in Members' communities.

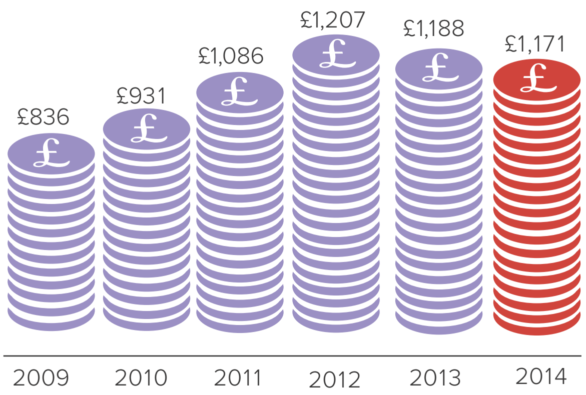
**Straightforward**
We always communicate clearly and offer uncomplicated products and services.

**Consistent**
Our Members depend on us for competitive, good quality products and services that meet their needs and reward their loyalty.

**Proactive**
By anticipating future developments and Member needs, we not only future-proof our business, but can take action to minimise negative consequences, seize opportunities and improve our Members' experience.

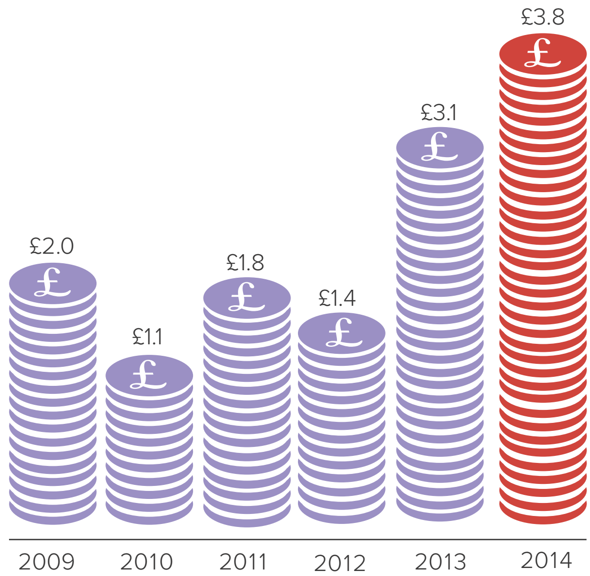
# CONTENTS

# FINANCIAL HIGHLIGHTS




## Group Assets (£m)

- Group Assets have reduced by 1.4% in the year.
- The Groups lending book has increased in the year by £57.4m (7%), reflecting the Society's record year for lending.
- Liquid Assets have reduced by £74.7m (23%) driven by the growth in the mortgage book and a reduction in corporate deposits.

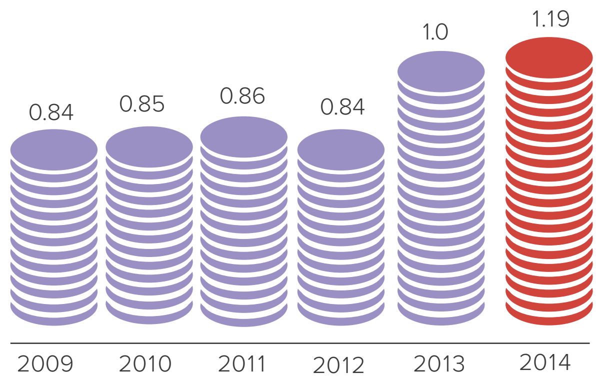



## Group Profit before Taxation (£m)

- Operating profit before provisions increased by £1.6m compared with 2013 due to enhanced underlying profitability.
- Provisions for bad and doubtful debts have been increased by £1.0m where the Society has decided to accelerate the resolution of those properties where the Society is currently acting as Receiver of Rents.
- Group profit before taxation has again been impacted by a Financial Services Compensation Scheme Levy (FSCS) of £0.8m (2013: £0.7m)


## Society Arrears Ratio (%)

- This ratio expresses mortgage balances in arrears as a % of the total Society mortgage book. It has been restated for all years to take into account a re-classification of the properties where the Group is the Receiver of Rents.
- The level has dropped slightly against 2013 (Restated) and is above the Prudential Regulation Authority's 2014 published equivalent of 1.40%.
- The Group arrears performance (greater than 3 months in arrears by number) at 0.79% (2013 Restated: 0.72%) is below the Council of Mortgage Lenders 2014 published average of 1.05%.




## Management Expenses (%)

- The ratio expresses management expenses of the Group as a % of average Group Assets.
- The ratio has seen an increase in 2014 to reflect investment in our people and technology which is designed to improve the service offered to our members, and the increased demands of regulation.
- The ratio is forecast to rise again in 2015 due to the investments being made in the people and technology.

# BUSINESS OVERVIEW

The Saffron Building Society Annual Report and Accounts 2014 reflect the aggregate results across the Society's business activities. Saffron's products and services are accessible to our Members in a variety of ways whether through our branches and agencies, our Contact Centre or online. The Society's business activities are as follows;

## Savings

The Society offers a wide range of savings and investment products. These include instant access, fixed term, tax free savings and children's savings plus longer term investments linked to the stock market.

Being a mutual means we put our Members first and we strongly believe in rewarding loyalty through existing customer only interest rates and Members' only products.

## Mortgages

In a diverse range of situations Saffron can help. Our 'Everyday Situations' range includes a choice of competitive mortgages which are ideal for customers buying a home, wanting to get on the property ladder or seeking a mortgage for a Buy-To-Let property.

The 'Special Situations' range can accommodate customers who require something out of the ordinary, contractors or self-employed, young professionals, those renovating a property or an unusual property type.

Whatever the situation, Saffron will take into account individual circumstances, apply common sense and provide a personal and reliable service.

## Financial Advice

Financial planning is about establishing goals and aspirations and working out the best way to achieve them. Through our relationship with Towergate Financial Limited we are able to offer our customers the opportunity to consider their aspirations and get advice on how best to achieve them.

We can offer help with:

- Investments
- Estate Planning
- Protection
- Will Writing
- Annuities
- Funeral Planning

## Insurance

We offer a wide range of general insurance cover through our independent insurance intermediary service rather than a single tie up with one insurer. Areas covered include:

- Motor
- Travel
- Home
- Commercial including Buy-To-Let

## Business

We offer a wide range of products from general savings for limited companies to accounts created especially for organisations like legal firms, charities and clubs.

We can also offer business protection, planning and pensions, working in partnership with Towergate Financial Limited and general insurance through our intermediary service.

# CHAIRMAN'S STATEMENT

GEOFFREY DUNN

I am pleased to report to our Members that 2014 was another very strong year for Saffron Building Society, with growth in net interest income and a significant increase in profits (before tax) to £3.8m. In line with the Society's plan for 2014, total assets have remained at £1.2 billion, as we have continued the traditional Building Society model – using savings deposits to fund residential mortgages, whilst retaining a prudent amount in high quality liquidity.

Even though 2014 has been highly successful, there have also been a number of challenges for the Society and its Members.

It was a successful year because we continued to deliver our core strategy of making a wide range of mortgages available to suitable applicants, whilst maintaining our long-term credit standards. In 2014, we advanced a new record amount of £240m and were the winner of the Moneyfacts Best Service from a Mortgage Provider, a real accolade when you consider our size and that we were up against the major high street lenders in this category.

At the same time, 2014 was a challenging year for many of our Members. The global (not just UK and Europe-wide) phenomenon of record low interest rates, will have had a continued adverse effect on many of our Members' incomes. The Bank of England rate is at a 300 year low and has not changed since March 2009. Notwithstanding these difficult market conditions for savers, we have continued to offer fair savings rates to Members, with five products across the range offering a top ten rate or better. We are very proud of the fact that the Society was first to market with a competitive regular saver NISA, which was launched just one week after HM Government's announcement regarding ISA changes. Given the current outlook for low inflation and slow economic growth in the Eurozone, it is very hard to see when interest rates will rise to more "normal", long-term levels for savers.

Despite the continued high demand for mortgages, we have continued to apply our consistently high credit underwriting standards, whilst also making substantial progress with the wholesale upgrade of our internal systems. As many of you will have personally experienced, our online savings capability has been materially improved. In 2015, we are continuing our program to improve and enhance our systems and later this year it should also cover mortgages and then, savings made through the branch network. These developments taken together with continued work to improve our service levels by phone or online or mobile, means that in the years ahead, Members will have a better choice of how and when they wish to deal with the Society. It should become a much more pleasurable experience.

2014 has been another year where our Regulators (the Prudential Regulation Authority (PRA) & Financial Conduct Authority (FCA) imposed a significantly enhanced Regulatory Agenda. By April 2014, the Society (in common with all other Building Societies) had to comply with the requirements of the new Mortgage Market Review (MMR). I am pleased to say we have been fully compliant with this initiative and continue to support the Regulators to ensure that we see a stronger and more resilient mutual movement emerge in the future. In 2015, it looks like the trend of increased regulatory oversight will continue.

2014 was also a challenging year insofar that there were several new "challengers" in the mortgage market plus the wholesale return of the high street banks, who had been quite subdued in this market, whilst they recovered from the financial crisis of 2007. The Society has also been focussed upon managing its liquid assets to reduce the negative carrying cost. This year, we have optimised these liquid funds through making record higher mortgage advances.

During the year investment continued to upgrade facilities for our people, with the much needed refurbishment of our Head Office at Saffron House. Continued tight management of expenses and strict adherence to our long-standing credit standards, combined with the use of the excess liquid assets has led to higher profitability up 18% to £3.8m, which has improved our capital position. This means greater security for Members, as well as helping us to meet our regulatory requirements.

We have also continued to work to improve all aspects of our Corporate Governance.

Last year, we advertised extensively to find three new Non-Executive Directors (NED). We were delighted to have found and recruited three very able and immensely experienced individuals, whom have brought renewed energy, challenge and professional insight to the Board.

Firstly, we have a new Chairman of the Risk, Audit, Conduct and Compliance Committee. Neil Holden is an accountant with significant experience of audit and control matters in banks and similar institutions. Secondly, we recruited Nick Treble with 30 years experience in treasury and related matters to ensure that every aspect of our asset and liability management is fit for purpose.

Finally, we persuaded Gary Barr, with more than 20 years experience delivering major IT and change programs in companies such as Morrisons and Dixons, to join us.

I am sure you will agree with me that these appointments will help ensure that the Board of Saffron remains well positioned to continue to make good progress.

This year we are continuing our search for two new NEDs to replace Directors who are due to retire (having completed the maximum term). We will continue to search further for high calibre women to join the Board and provide further diversity of insight and perspective to the Board and leadership of the Society.

I am hopeful by the time of the AGM, I will have some positive news to advise members.

## Leadership changes

In May, Chris Plumbridge the Finance Director (FD), retired and was succeeded by Colin Field, who had previously joined us as Group Financial Controller. Colin was already very experienced in financial services having been with Barclaycard and other companies. As Chief Financial Officer, he has already made significant progress in upgrading our financial reporting and management.

Sarah Howe was also appointed to the Board in May as Chief Customer Officer, having joined the Society as Chief Marketing Officer in 2013. Sarah is responsible for products, services and customer experience delivery, through both the retail network and our contact centre for both Members and brokers. Sarah has extensive customer and brand experience both in financial services and in membership-based businesses such as BUPA and Ageas.

In October, Jon Hall the Chief Executive Officer, resigned after 10 years with the Society. Jon was initially appointed as our FD and then later as our CEO. We wish Jon well in his future career.  We are actively searching for a new CEO to continue to take the Society forward and by the time of the AGM we hope to be better placed to update Members on progress.

Given the number of major initiatives under way within the Society, the Board felt that it would be inappropriate to place the additional burden of assuming the Interim CEO role on any one of our existing leadership team, so we have recruited a highly experienced Interim CEO, Mike Kirsch, who will ensure the Society remains on track and delivers all the planned developments.

Towards the end of 2014, we retendered the contract for the provision of Internal Audit Services, which was won by PricewaterhouseCoopers (PWC), replacing KPMG. I would like to thank KPMG for their contribution to our control environment and for the assurance services, they have provided to the Society over many years. We look forward to working closely with PWC from 2015.

During the year, we also appointed a new Chief Risk Officer, Fraser McNeill who together with our CFO, Colin Field, have helped the Society upgrade much of its regulatory reporting and compliance.

Finally, I would like to give a very special thanks to all of our staff, who by their actions and behaviour, make Saffron the Society that you, our Members, would wish it to be.

## Outlook

The combination of a UK General Election, enormous geo-political uncertainty, rapidly falling oil prices, coupled with continued Eurozone economic stresses means that 2015 presents a highly challenging external environment for the Society.

We shall continue to do what we have always done, concentrating the majority of lending into our local region and also London and the South East, whilst attempting to attract and retain high quality customer deposits.

In other words, become “The most recommended Building Society”.

Geoffrey Dunn

GEOFFREY DUNN
Chairman

# BUSINESS MODEL AND STRATEGY

## The Group's business

The Group's business is to make loans that are secured on residential property and funded principally by its Members. It also offers savings and deposit products and other, non-interest earning products (for example, insurance) through third party specialist, product providers.

It is run through its Head Office in Saffron Walden, Essex; Customer Contact Centre in Great Chesterford; and, 12 branches across East Anglia.

### The Group's income

The Group's income is derived from interest, fees and similar charges arising from its investments in loans secured on residential property.

It also earns interest on its liquidity portfolio and fees and other income from its third party, specialist, product operation.

### Generation of assets

The Group generates new assets through originating new mortgage loans secured on residential property.

In the past, the Group also generated new assets through the acquisition of mortgage portfolios by its Crocus subsidiary. At the moment, the Group currently holds approximately £47m of lifetime mortgages but has no plans to expand this activity.

The Group continues to keep the mortgage market as a whole under review to consider whether lending in any new product areas should be introduced in accordance with the Group's stated risk appetite.

### Funding the business

The Group's main source of funding for its originated assets is retail savings and deposits.

This is supplemented, where appropriate, by corporate savings and deposits (for example, solicitors' client money) and limited use of wholesale facilities.

### Profitability of the business

The profitability of the business relies on:

- careful management of loan accounts to increase retention and maintain the current low levels of delinquency;
- vigilance in the underwriting processes to mitigate losses;
- appropriate pricing of new advances;
- delivery of effective customer service;
- arranging appropriate funding sources to sustain the business; and,
- maintaining control of operating and investment costs.

## Principal risks and uncertainties

There are a number of potential risks and uncertainties which could have a material impact on the Group's performance and could cause actual results to differ materially from expected and historical results.

In order to ensure that the interests of all Members are adequately protected at all times, it has established and embedded a robust governance structure and risk management framework that are designed to identify, manage, monitor and control the major risks exposed in the delivery of the Group's strategic objectives.

The principal risks that arise from the Group's operations are credit, treasury, operations, strategic and external risks. These key categories of risk are common to most financial services organisations in the UK and the Group aims to follow best practice in this area and to manage the associated exposures within its stated risk appetite.

### Risk management framework

The oversight and direction of the Board is central to the Group's risk management framework.

It ensures, through a series of Board sub-committees and management structures, that appropriate policies, procedures and processes are implemented across the business to control and monitor risk exposure in accordance with the Group's stated risk appetite.

The framework identifies operational roles and responsibilities (both individual and collective) in the risk management process and ensures that exposed risks are aligned to the Risk Appetite Statement of the Board, with any unacceptable risk exposures being managed and mitigated.

Each of the Board sub-committees includes at least two Non-Executive Directors, with other committee members drawn from the Executive and appropriate members of senior management.

The key risk orientated committees, operating under the delegated authority of the Board, include the Risk, Audit, Conduct and Compliance Committee (RACCC), Assets and Liabilities Committee (ALCO) and Credit Committee.

The principal risks inherent in the Group's business model include the following:

### Economic environment

All aspects of the Group's business are exposed to risk from the UK's general economy.

Adverse economic conditions (for example, house price falls, rising unemployment, rising interest rates) might increase the number of borrowers that default on their loans or adversely affect funding structures, which may in turn increase the Group's costs and could result in losses on some of the Group's assets or restrict the Group's ability to develop in the future.

The general economic factors affecting the Group going forward, together with the steps taken by the Group's management to address these issues are described in the Chairman's Statement and Chief Executive's Review.

Changes in interest rates may adversely affect the Group's net income and profitability. The steps taken by the Group's management to mitigate against the long-term effects of

# BUSINESS MODEL AND STRATEGY

interest rate movements are described in Note 25 to the Accounts.

**Credit risk**

As a primary lender the Group faces credit risk as an inherent component of its lending activities.

Adverse changes in the credit quality of the Group's borrowers, a general deterioration in UK economic conditions or adverse changes arising from systematic risks in UK and global financial systems could reduce the recoverability and value of the Group's assets.

The Group's approach to the management of credit risk and the systems in place to mitigate that risk are described in Note 12 to the Accounts.

**Funding risk**

The Group relies on its access to sources of funding to finance the origination of new business and working capital. If access to funding became restricted, either through market movements or regulatory or Government action, this might result in the scaling back or cessation of new lending.

The Group, through ALCO, seeks to mitigate this risk by managing effectively the Group's liquidity portfolio and actively seeking alternative sources of finance (for example, through the Bank of England discount window facility) and keeping its funding and working capital position under review.

**Operational risk**

The activities of the Group expose it to operational risks relating to its ability to implement and maintain effective systems to process its transactions with Members and customers. A significant breakdown in IT systems of the Group might adversely impact the ability of the Group to operate its business effectively.

To address these risks, the Group's Chief Risk Officer (CRO) and his team and the Group's internal audit function carry out targeted reviews of critical systems and processes to ensure that they remain adequate for their purpose.

The Group has a Business Continuity Plan which is kept under regular review and is designed to ensure that any breakdown in systems would not cause significant disruption to the business.

**Competitor risk**

The Group faces competition in all the core markets in which it operates. There is a danger that its profitability and/or market share may be impaired.

To mitigate this risk, the Group maintains close relationships with its Members and customers, business introducers and other significant participants in the markets in which it is active as well as participating in sector-wide organisations (for example, the Building Societies Association) and initiatives.

This allows market trends to be identified and addressed within the Group's business strategy.

**Government, legislative and regulatory risk**

The market sectors in which the Group operates and the markets from which it receives its funding have been subject to extensive intervention by the UK Government, European Union and other regulatory bodies.

To the extent that such actions disadvantage the Group, when compared to other market participants, they represent a risk to the Group.

In order to mitigate this risk, the Group has been active in explaining its position to the authorities and has engaged its professional advisers in this process.

Moreover, in order to ensure compliance with the various regulatory regimes that the Group is, or may become, subject to, the Group maintains a compliance function within its Risk management team and this activity is also subject to the review and scrutiny of the Group's RACCC.

**Management**

The success of the Group is dependent on recruiting and retaining skilled senior management and personnel and failure to do so would put the Group's ability to carry out successfully its plans at risk.

The Group's employment policies are designed to mitigate this exposure and to ensure that an appropriately skilled workforce is, and remains, in place.

**Other financial risks**

The Group's exposure to other financial risks, including liquidity risk and the procedures in place to mitigate those risks are set out in detail in Note 25 to the Accounts.

**Uncertainties**

For 2015, the principal uncertainties faced by the Group are associated with the outlook for financial markets, the UK economy and continuing changes in the regulatory regime.

These include:

- whether recovery in the UK housing market continues through 2015 and beyond;
- maintaining a competitive savings offering to Members against the background of flat interest rates (created (in part) by the Government's Funding for Lending Scheme);
- the continuing impact of an uncertain economic growth outlook on unemployment levels combined with consumers being squeezed with higher living and mortgage costs; and,
- the deployment of changes to the regulatory structure, which will have a significant impact on the financial services sector including the changes set out in the Capital Requirements Regulations under the Basel III regulatory regime and the Senior Management Regime.

The Board makes sure that the focus remains on serving Members' best interests whilst ensuring that the Group remains compliant, effective and efficient.

# CHIEF EXECUTIVE'S REPORT

MIKE KIRSCH

*"Friendly, knowledgeable staff and competitive products from a Building Society that is big enough to give good value but small enough to still value its customers."*

*"Always great customer service - everyone has sunshine in their voices!"*

*"Outstanding personal service which other banks/societies could learn from."*

These were just three of the comments received from Members this year which I particularly like as they encapsulate and reflect the Society's emphasis on the long-term and importance placed on family and the continued value of personal expert service.

As your Interim CEO who has been in place since November 2014, I am delighted to say that everything I have found is entirely consistent with the above. The Saffron Building Society really does focus on its Members, cares deeply about doing its best for Members through its products and services; and is committed to continuing to do so over the long-term in its own valued and friendly way.

2014 was a good year for the UK economy, and a good year for the housing market. It was also a record year for the Society for which the leadership team deserve a lot of credit. As outlined by the Chairman, profits are critical both to the generation of surplus capital and for ensuring the ongoing strength of the Society. A profitable Society is best placed to serve its Members over the long-term.

Although housing market activity has been cooling and house price growth slowing in recent months, 2014 was still the strongest year for mortgage lending since 2008. It is particularly pleasing to see the strong increase in the number of first-time buyers who played a key role in the market growth. First-time buyers were clearly encouraged and helped by government initiatives such as Help-to-Buy. As a result, the number of first-time buyers topped the 300,000 mark. While a far cry from the half million that we might regard as 'normal', this was the highest number of first-time buyers since 2007.

It was not such a good year for savers owing to the ongoing Bank of England policy of low base rates. Competition for savings was limited in 2014 with Moneyfacts data showing that average savings rates fell again. The one year average ISA rate for example being just 1.46%. With inflation falling throughout 2014, and with the potential for the UK to move into a period of deflation as we enter 2015, the small consolation for savers is that inflation is no longer eroding the value of your savings and interest income. We are however doing our best for our saving Members and this is highlighted through our 'Savings Promise' As I note later the Society is, through our 'Savings Promise', consistently providing a good range of savings products for our Members and will continue to do so in the future.

During 2014, the Society dealt effectively with the increasing demands associated with the regulatory environment, as evidenced by the successful implementation, in April, of the Mortgage Market Review regulations, along with continuing to effectively manage the relationship with both of our regulators – the PRA and the FCA.

As well as ensuring we fully satisfy the requirements of our regulators, the Society has been investing to ensure it is fully fit for the future and can also satisfy the future needs of our Members and business partners. This investment is principally being made in two areas, notably increasing the management and technical skills capability of the organisation as well as bringing our business systems up to date. Attracting and retaining good managers and technical experts given the size of the organisation and proximity to London is a constant challenge. The Society is committed

MIKE KIRSCH
Interim Chief Executive

# CHIEF EXECUTIVE'S REPORT

to having the permanent management capability to ensure we continue to be successful into the future. This will be one of the key tasks for the new CEO, whenever he or she is appointed later this year.

We began the process of fundamentally upgrading our business systems with the introduction of our new online savings system in 2013. Since then we have been developing our new mortgage system which we will begin to roll out in March 2015. The first stage of this progressive roll out will be for processing of new mortgage business. Our intention is to ultimately include a portal which will enable our business partners to submit applications online. Once implemented this will be a major step forward for the organisation and how it deals with its mortgage introducers. Our plan is to commence the servicing of these mortgages on the new system around the middle of the year, to be followed by the migration of our existing mortgage book onto this system before the end of 2015. The last stage of our IT transformation programme involves updating the systems we use to support our branch operations, which will probably take place in 2016.

As you can see we have a deliberate strategy to incrementally roll out these new systems. This is to ensure we appropriately manage the risks which are always inherently associated with new IT systems, and equally importantly to ensure our service and customer satisfaction levels remains very high. For most of our Members these changes should hopefully not be apparent and in fact be seamless.

Once the complete IT Business Systems change programme is fully implemented in 2016, the Saffron's core operating systems should have been brought fully up to date and be capable of supporting further business growth.

Similar to last year the Board assesses the performance of the Society on a balanced basis, using measures in four areas:

- 'Financial': improving financial strength and generating a return on resources;
- 'Members and Customers': generating Member value and customer satisfaction;
- 'Internal Quality and Risk': maintaining the Society's reputation as a trusted provider of products and services and ensuring that we are operationally effective; and,
- 'Our People': our people are engaged and committed.

For 2014 these are reviewed separately below.

## Financial

### Profit

Group operating profit (before tax) in 2014 was £3.8m (2013: £3.1m). Statutory profit after tax in 2014 was £3.0m. The major contribution to this performance was a significant improvement in net interest income (Net Interest Margin 2014: 1.60%, 2013: 1.18%). This has been achieved by converting liquidity previously invested in low yield treasury assets into profitable mortgage lending.

Gross mortgage completions of £240m represented a record year for the Society as did the gross lending of £901m. Additional services such as independent financial advice and help with estate planning have continued to be well supported in branch by our Members, but the financial performance of our insurance service has continued to decline and we are currently looking to reinvigorate this offering.

The higher levels of income were partially offset by a rise in administrative expenses. Your Society, in common with others continues to face increased costs from regulation and the necessity to exhibit greater depth and breadth of management and technical capability across the organisation. The Society has continued to invest in additional people and infrastructure that will ensure that our organisation remains fit for purpose and able to handle future challenges.

The leadership team have focussed hard on improving the composition of the Balance Sheet, specifically increasing the level of net lending whilst reducing the level of excess liquidity that has restricted the returns that the Society has made in recent years. Whist this focus has been successful, the static Balance Sheet size and increase in the expense base has meant that the management expense ratio has increased to 1.19% of average assets – above the 1% level that historically has been the benchmark for Building Societies. I would expect to see this pattern of increase reflected in the results of a number of Societies in 2014 as they, like us respond to the challenges that are presented to the sector. I would expect the expense ratio to increase further in 2015 as the full costs of the investments are recognised by the Society.

In line with all building societies, your Society, as a retail depositor funded business, bears a disproportionate cost under the Financial Services Compensation Scheme (FSCS). The building society sector continues to campaign against the unfair burden for Societies and their members, who ultimately pay for the levies to the FSCS. The 2014 cost was £0.8m (2013: £0.7m).

The rise in general bad debt provisions to £4.0m (2013: £3.0m) appears contrary to the continued consistent underlying levels of arrears experienced by the Society. The Society has taken the strategic decision to accelerate the resolution of those properties where the Society is currently acting as Receiver of Rents and this in turn has led to a greater provision being held.

### Assets

The slight fall in assets in 2014 represents a continuation of the strategy highlighted in the 2013 Report and Accounts for the Society to maintain lower liquidity levels, increase levels of profitability and improve further the capital surplus.

# CHIEF EXECUTIVE'S REPORT

**Capital**

The Group, as 31 December 2014, had total regulatory capital resources (being total capital, excluding pension reserve plus general provision for bad and doubtful debts) of £62.2m or 16.5% (2013: £59.3m or 16.2%) of risk weighted assets in accordance with the European Capital Requirements Directive, commonly referred to as Basel III.

## Members and Customers

Once again it has been another difficult year for savers seeking to maximise their savings income. A continuation of the low interest rate environment driven by the economic uncertainty in Europe has resulted in the Bank of England base rate at an all-time low coupled with falling inflation creating further concerns about when an interest rate recovery will be on the horizon. The emergence of new 'challenger' banks has in part contributed to more volatility in rates as they competed for current accounts and savers deposits. The Society has remained focussed on providing stable and reliable long term rates with an ambition to be in or near the top ten rates available in the market for key savings accounts. Our progress has been charted through the year through the introduction of our Society 'Savings Promise' which is published quarterly and available online and in branch, demonstrating the rate performance of key society savings products versus the market.

I am pleased to say that the Society has remained a top 10 provider with the popular Regular Saver account (commended by the Guardian and Money Observer as 'Best Adult Regular Saver product'), our re-launched Children's account, the e-saver 3 and the Members' maturity bond. In April we launched a Regular Saver NISA for Members which was a market first, enabling Members to take advantage of the newly announced increased NISA limits. A 4 year Stepped Bond and NISA was launched in October which achieved best buy status. In all we only made 3 rate changes to Member products based on market conditions, one of which was a rate increase, introduced market leading products and appeared in best buy tables 26 times through the course of the year.

The Free Savings Review remains central to the Society's customer proposition and in all we conducted just short of 9,000 reviews in the year. At a time when savings choices can be confusing with the introduction of NISAs and current changes to the pensions market, more options are available for our Members. We believe we play an important role in helping guide Members to make decisions about their financial options aligned to their short, medium and long-term goals. We retain our Fairbanking status for the goal saver account and will be looking to make further progress and enhancements in 2015.

Our Members are the heartbeat of the Society and as such we rely on Member feedback and help in shaping solutions and new initiatives. We held a Member event in June where Members were invited to tour the new premises in Little Chesterford; we discussed the Saffron customer service model. In October we invited a selection of Members, non-Members and staff to help us design a new branch environment that would better serve the needs of new and existing Members. It was a hardworking and engaging day with attendees of all ages from 18 to 80 designing and presenting their ideas. The good news is that across generations there are very consistent needs and desires and we aim to unveil the final design in our new branch location in Colchester during 2015.

Based on their success in 2013, we continued holding evening seminars in selected branches to offer customers access to advice on retirement planning. The events have been well attended and feedback was very positive with more events being planned.

Customer satisfaction remains central to our ethos and yet again we had exceptional scores with almost 9 out of 10 customers surveyed saying they are very satisfied with the Society. Feedback was overwhelming regarding the excellent standards of service our people deliver to Members every day. The branches offer such a personal and valued service that on 4 occasions we achieved a perfect 100% customer satisfaction score which is an outstanding achievement. The Royston branch achieved the accolade of being the 2014 branch of the year which was very well deserved by Karen Barker and her team.

The new Mortgage Market Review regulation came into force in April and Saffron launched new processes and affordability checks ahead of the regulator's deadline with a smooth transition for brokers. We had a record breaking year for mortgage lending completing over £240m in new mortgages helping more than 900 customers buy their home. We were delighted to be crowned the winner of the prestigious Moneyfacts Best Service from a Mortgage Provider and have once again been nominated for an award in 2015 for Best Specialist Lender with results due in February.

## Internal Quality and Risk

Effective risk management, including a critical focus on robust conduct risk management, is central to our primary objective of protecting the security of Members' money. Details on our approach to risk management are contained within the Business Model and Strategy section of the Group's Business Review and in our Capital Report (Pillar 3 disclosure) which is available online in the Members' area of our website.

Ultimately asset quality will be demonstrated in arrears performance on mortgages and avoiding losses on treasury investments. We believe mortgage lending and treasury investment should be consistent with our Building Society heritage and straightforward to explain to our Members.

This is reflected in a continuing focus on residential mortgages with our lending centred mainly in the East of

# CHIEF EXECUTIVE'S REPORT

England, South East and London. We have worked hard to ensure that our mortgages perform well and our arrears performance of 1.51% of Society mortgages is a testament to that work and the quality of our underwriting and mortgage lending.

Saffron continues to operate a very conservative approach to treasury investments with a stringent counterparty list and high levels of realisable investments controlled by the Head of Commercial Finance and Treasury. We are pleased to report, as in previous years, no losses on treasury holdings.

We have received a very low level of complaints during 2014. We undertake analysis of the cause of all complaints to make sure the highest standard of service is delivered to our Members. Our continued investment in our systems and resource capability demonstrate our commitment to delivering a high standard of service to our Members.

## Our People

As a new CEO to the business, the commitment of our staff to Saffron and our Members has made a real impact on me. In what has been another successful year, our staff have once again stepped up to deliver quality of service to our Members to underpin our financial results.

To ensure our staff are provided the right tools to develop in their current role and future career, Saffron remain committed to the investment in our people. This past year we have continued our focus on the development of their knowledge and skills across many areas and disciplines.

During 2014 we introduced business wide initiatives designed to build staff capability and to enhance the customer experience; including, for example, a development scheme framework aimed at tailoring personal development for all staff. In an ever changing world we also introduced our staff to an "understanding change" programme. This is designed to help our staff understand and respond positively to changes in the financial services environment, and also to provide a reference to understand changes from their own personal perspective.

Saffron remains committed to providing a positive and rewarding career development experience for our people. We are fortunate that many staff have chosen to work with us for a significant part of their careers but, regardless of their time with us, our aim is to help all to be the best that they can be.

## Community

It remains very important to us to give back to our community.

We do this in a number of ways – through donations to good causes made via our own Community Fund, by taking part in local activities and by fund raising for charities close to the hearts of our staff.

In 2014 we sponsored and took part in various activities as part of Saffron Walden's carnival week. We raised over £5,700 through fundraising events undertaken by staff such as our ever popular Staff Quiz, themed dress down days and cake sales.

In addition our Community Choir based in Saffron Walden has gone from strength to strength and even had the privilege of singing at the West Road Concert Hall in Cambridge with other community choirs. The essence of community is embodied in the Choir; with participation, both actual and encouraged, by our staff, our Members and others from the local community.

## Looking Forward

The Society is well placed and has clear plans in place to succeed in the future. I am very confident that it will continue to serve well the interests of its Members and other stakeholders.

On a personal note I will be very sad to step down when the permanent CEO arrives. I think Saffron is a good regional Building Society which really does help its Members. The UK mortgage and savings market is much better for having Societies such as ours playing a small but important role. We certainly add diversity and choice, as well as helping to keep some of the bigger players honest. I would like to take this opportunity to thank the management, staff and the Board for all their hard work and support through my short period of stewardship and wish them and the Society all the best for the future.

Mike Kirsch

Mike Kirsch
Interim Chief Executive

# GOING CONCERN

Corporate governance 'best practice' requires those charged with the Group's corporate governance to satisfy themselves that the preparation of the Group's Annual Report and Accounts using the going concern basis is appropriate.

Specifically, the Directors' statutory responsibilities in terms of forming a judgement as to whether a company is a going concern and ensuring that the Directors carry out an appropriate assessment of going concern for the purposes of being able to approve the Annual Report and Accounts.

The activities of the Group, its current operations and those factors likely to affect its future results and development, together with a description of its financial position and funding position are described in the Chairman's Statement and the Chief Executive's Review.

The principal risks and uncertainties affecting the Group and the steps taken to mitigate these risks are described in the Group's Business Model and Strategy.

As described in the Group's Business Model and Strategy, the Group has a formal process of budgeting, reporting and review. This provides information to the Directors which is used to ensure the adequacy of resources available to the Group to meet its business objectives.

This process covers (amongst other things) the economic backdrop to the Group's activities (for example, the growth in the UK GDP and the Bank of England's 'forward guidance' on interest rates); the Group's liquid resources; the Group's capital resources; and the Group's profitability.

Other considerations include the impact of a significant change in the basis of providing for amounts due under the Financial Services Compensation Scheme (FSCS); further, material changes in the regime for the regulation of the Group's capital (commonly known as Basel III); and further financial market stresses leading to significant capital issues amongst UK banks and a reduction in liquidity in the UK financial system.

After making the necessary enquiries, the Directors have a reasonable expectation that the Group will have adequate resources to continue in business for the foreseeable future and on this basis they continue to adopt the going concern basis in preparing the Annual Report and Accounts.

# APPROVAL OF BUSINESS REVIEW

The Society aims to follow best practice in the layout and contents of its Annual Report as well as meeting the requirements of the Building Societies Act.

Accordingly the Society has included a Business Review (equivalent to a Strategic Report under Companies Act legislation) comprising Chairman's statement, Business Model and Strategy, Chief Executive's Review, and Going Concern Statement.

The Review has been prepared for the Group as a whole.

Approved by the Board of Directors and signed on behalf of the Board.

Geoffrey Dunn, Chairman
5 March 2015

# CORPORATE GOVERNANCE REPORT

The Board of Directors is responsible for providing leadership and setting the strategic direction of the Society within a framework of prudent and effective controls which enable risk to be assessed and managed in accordance with the Board's stated risk appetite.

This report provides Members with information on the Society's Corporate Governance framework. The Society has regard to the UK Corporate Governance Code to the extent that it is relevant to a Building Society.

## LEADERSHIP

### The Board

It is the Board's role to set the strategic aims, ensure that the necessary financial and human resources are in place to meet the objectives and review the performance of the Executive team. The Board also puts in place a framework to enable risk to be assessed and managed in accordance with its stated risk appetite. At the end of the year the Board consisted of two Executive Directors, an Interim Chief Executive Officer and six Non-Executive Directors whose role is to provide independent challenge.

The Board meets at least 11 times a year and has a formal calendar of items for review. The Board retains certain powers for decision making but also delegates certain responsibilities and powers to Committees which are listed below. The Chairman holds meetings at least twice a year with the Non-Executive Directors without the Executive Directors being present.

The Chairman is responsible for the leadership of the Board and its effectiveness.

The Society maintains liability insurance cover for Directors and Officers.

The Board has established Committees to consider certain specialist areas in more detail than would be possible at a Board meeting. Each Committee operates within defined terms of reference. Minutes of meetings are formally recorded and proceedings are reported to the full Board by the respective Committee Chairman. The Committees and their summary terms of reference are set out below. The full terms of reference may be obtained through the Society website or on request from the Society Secretary.

### Remuneration and Loans Committee (Board Committee)

This Committee comprises all the Non-Executive Directors and is chaired by Jan Smith (Non-Executive Director, Vice Chairman and Senior Independent Director). It sets remuneration policy for Directors and reviews and approves remuneration arrangements and service contracts for Executive Directors as well as Directors' fees. The Committee takes responsibility for monitoring compliance with the regulatory Remuneration Code as it applies to Code staff. It also considers and approves loans to Directors or connected persons. The Committee meets at least twice a year to review remuneration and as necessary to approve applications for Directors' loans.

### Nominations Committee (Board Committee)

This Committee consists of the Chairman, Vice Chairman and Chief Executive and is chaired by Geoffrey Dunn (Society Chairman). The Committee reviews the balance of Board skills, independence, experience and knowledge, its structure and composition, any new appointments and the performance of Directors. It decides the membership of Committees. The Committee also ensures that the Society meets its statutory responsibilities in respect of compliance with the Building Societies Act and follows good practice in Corporate Governance, including reviewing the UK Corporate Governance Code. In the appointment of new Directors the Committee focuses on the need for diversity around the Board table and uses a professional search firm or open advertising to encourage applications from a range of candidates. The Committee considers diversity in the context of experience, background and skills as well as gender and ethnicity.

### Risk, Audit, Conduct and Compliance Committee (Board Committee)

This Committee comprises nominated Non-Executive Directors, excluding the Chairman, and is chaired by Neil Holden (Non-Executive Director). Members of the Executive are invited to attend as appropriate. The Committee reviews the effectiveness of the Group's systems of internal control and monitors compliance with regulatory requirements and relevant codes of practice. It considers and approves the remit of the risk and compliance management functions and provides input, review and challenge to executive management's identification and assessment of risks. It ensures that either the Society remains within its risk appetite and tolerances in the various aspects of its business or that management takes appropriate mitigating actions where the risk appetite is being, or appears to be at risk of being, breached.

It approves the annual integrated assurance plan comprising the internal audit and risk management and compliance plans. These activities are based on a thorough risk assessment of the full scope of the Group's business activities. The Committee meets at least quarterly and monitors progress. All Non-Executive Directors on this Committee have experience that is relevant to the role

# CORPORATE GOVERNANCE REPORT

and at least one member present has recent financial experience.

During 2014 the Committee met nine times to fulfil its responsibilities and, in particular, considered reports for the following:

- the effectiveness of the system of internal control;
- the integrity of financial statements;
- the activities of internal audit, external audit, Risk and Compliance teams;
- the performance of the external auditor and its independence, objectivity and effectiveness;
- technology risk;
- risk appetite, maturity and culture; and,
- regulatory compliance and reporting including Conduct Risk and Treating Customers Fairly.

### Assets and Liabilities Committee (Management Committee)

The Committee comprises Executive Directors, the Chief Risk Officer, Head of Commercial Finance and Treasury. Two named Non-Executive Directors also attend meetings. It recommends treasury and Balance Sheet risk management strategies, capital requirements in the context of the Society's policy statement concerning liquidity, funding and structural risk management policies. The Committee meets at least 11 times a year and is chaired by the Chief Financial Officer.

### Credit Committee (Management Committee)

The Committee comprises Executive Directors and three named Non-Executive Directors who also attend meetings. The Committee reviews lending propositions and loan performance as well as benchmark and trend data. It reviews and recommends to the Board changes to lending policy or limits. The Committee meets at least 11 times a year and is chaired by the Chief Risk Officer.

Current membership of the Committees and attendance for all Directors is shown on page 16.

### Roles of the Chairman, Non-Executive Directors and Executive Directors

The Society maintains a clear division of responsibility between the Non-Executive Directors and Executive Directors and these are outlined in job descriptions and a table of delegated powers.

The Executive Directors are expected to manage the Society under the strategic direction of the Board as a whole.

The Chairman and Vice Chairman are elected by the Board on an annual basis.

The Chairman sets the governance agenda, standards and expectations for Board Directors and ensures constructive challenge and openness between Non-Executive and Executive Directors.

## EFFECTIVENESS

### Board balance and independence

The Board is currently composed of six Non-Executive Directors, two Executive Directors and the Interim Chief Executive Officer. In addition other Executives are invited to attend Board meetings as needed.

The Board considers that all Non-Executive Directors are independent in character and judgement.

The Chairman Geoffrey Dunn has served four years on the Board and was elected as Chairman in 2014. The Vice Chairman, Jan Smith, has served nine years. Charles Wilson has served six years on the Board. Three new Non-Executive Directors: Gary Barr, Neil Holden and Nick Treble are seeking election at the AGM; each has served one year on the Board. Details setting out why each Director is deemed to be suitable for election have been included with the Notice of Annual General Meeting issued to all members in the AGM mailing documentation.

### Appointments to the Board

The Nomination Committee leads the process for Board appointments and makes recommendations to the Board. The Board maintains a succession plan and produces a specification for vacancies to be filled.

The Board advertises externally or uses an external search consultancy for candidates for Board appointments. Members can nominate their own candidates for appointment subject to Society rules. The appointment of Directors is based on objective criteria including the ability to meet the requirements of the regulatory approved person's regime. Board succession planning ensures that the appropriate mix of skills, experience, independence and knowledge of the business is represented on the Board and Committees to enable them to discharge their respective duties and responsibilities effectively. The recruitment of new Non-Executive Directors is delegated to the Nominations Committee, which ensures that Directors are able to commit the time required to effectively fulfil the role, at the time of appointment and on an ongoing basis.

In 2014 the Board has increased the number of Directors by appointing Sarah Howe as Chief Customer Officer.

### Directors' interests

Directors are required to disclose any relevant external interests that may be considered to conflict with their role at the Society, including any other Directorships that they may hold at recruitment. There is also a formal process, which requires Directors to re-affirm their external interests annually. Furthermore at each Board meeting Directors are required to disclose any changes to their external interests. In all cases the Board considers if a Director's ability to act in the best interests of the Society might be compromised. No Director is counted in a quorum in respect of any own

# CORPORATE GOVERNANCE REPORT

conflict situation. Were a business relationship to exist between the Society and a company associated with a Non-Executive Director all dealings would be undertaken at arms-length.

### Information and professional development

Board reporting is of a high standard with an annual review of the scope and appropriateness of the information. More detailed reporting is provided to Board Committees and this is also provided to all Board members for information.

Non-Executive Directors attend internal and external training sessions, including Building Societies Association seminars and conferences, and receive copies of industry circulars and regulatory publications to further their knowledge. Training is tracked and records are held centrally. An induction programme is in place for all new Non-Executive Directors to ensure that they can provide effective challenge as soon as possible after appointment. Training and development needs are identified as part of the annual review process undertaken by the Chairman.

### Performance evaluation

The Board operates an annual appraisal scheme in which all Directors appraise the performance of each of their colleagues, including the Chairman, with the consolidated results also being used to evaluate any overall weaknesses. The results of the exercise inform the decision to recommend a Director for re-election.

The Board calendar includes a yearly review of Board and Committee effectiveness.

In 2014 the Nominations Committee recommended an external evaluation and Warren Partners who have no connection to the Board were commissioned to carry out this survey.

### Re-election policy

The Directors are subject to election at the first AGM after their appointment. A Non-Executive Director will normally serve for two terms of three years, with a maximum of three terms if there has been a significant change in role. The Nominations Committee reviews the performance of Directors before recommending them to stand for re-election. This includes a review of an individual's performance, and also considers if it is appropriate, to ensure the Board remains fresh and vigorous.

## ACCOUNTABILITY

### Financial and business reporting

The Directors' responsibilities for financial reporting are described in the Statement of Directors' Responsibilities on page 20.

### Internal control and risk

The Board is responsible for determining the risk appetite it is willing to take in achieving its strategic objectives and it reviews the processes and procedures to ensure sound risk management and internal control systems are in place. Senior management are responsible for designing systems to identify and control risk and ensure the Board is sighted on risk management through a quarterly review programme which is open to challenge. Internal audit provides an independent confirmation to the Risk, Audit, Conduct and Compliance Committee that appropriate procedures are in place and are being followed. The Board receives a formal annual report of the effectiveness of systems and controls from the Risk, Audit, Conduct and Compliance Committee. The Board has satisfied itself that a strong culture of compliance operates and that the systems are effective and appropriate given the nature of the business activity undertaken.

### Audit

The Board has established a Risk, Audit, Conduct and Compliance Committee. The work of this Committee is described on page 13.

The appointment or re-appointment of external auditors is recommended by the Risk, Audit, Conduct and Compliance Committee and confirmed by the Board. The Society is recommending to Members at the forthcoming AGM that Deloitte be re-appointed as Auditors.

Non audit services totalling £37,000 have been provided by Deloitte in the year. For each assignment the independence of the auditor is considered. At no point has the auditor been involved in management functions, decision making or assuring the adequacy of internal controls or reporting.

## REMUNERATION

The Directors' Remuneration Report on page 17 details the Board position on the UK Corporate Governance Code principles related to remuneration issues.

## MEMBER ENGAGEMENT

As a mutual the Society does not have shareholders but is responsible to its Members.

In 2014 informal Member group meetings were hosted by the Executive Directors to meet with and gauge the views of Members on issues that affect them.

Considerable work has been done to extend communication with Members through the Net Promoter Score system in branch, and online and the Members' panel.

Non-Executive Directors spend time in the branches and the Contact Centre on an annual basis to help them understand the Member perspective.

# CORPORATE GOVERNANCE REPORT

## Constructive use of the Annual General Meeting (AGM)

Details of the AGM are mailed to all Members who are encouraged to attend or to vote on resolutions. Prepaid envelopes are included to enable Members to appoint a proxy to vote on their behalf if they are unable to attend. The proxy form provides the opportunity to formally abstain from resolutions should the Member so wish. Information on voting is published on the Society website after the AGM.

As a further encouragement to vote the Society will be donating 20p to charity for every vote cast. Voting is made easier with an online voting option.

At the AGM the Chairman calls for a poll on all resolutions so that all proxy votes are recorded. A separate resolution is proposed on each issue including adoption of the Report and Accounts.

## Society Rules

A copy of the rules which were updated on 1 July 2014 is available on the Society's website www.saffronbs.co.uk, or may be obtained by a Member on request to the Secretary, Saffron Building Society, Saffron House, 1a Market Street, Saffron Walden, Essex, CB10 1HX.

## Directors' attendance at meetings 2014:

| Name | Board | Risk, Audit Conduct & Compliance | Remuneration & Loans | Assets & Liabilities** | Credit** | Change** | Nominations |
|---|---|---|---|---|---|---|---|
| Number of meetings held | 11 | 7 | 5 | 11 | 11 | 11 | 3 |
| T G Barr | 11 | 7 | 5 | 1 | 1 | 11 | n/a |
| T J Bayley *** | 4 | 2 | 2 | 4 | n/a | n/a | n/a |
| G R Dunn | 11 | 7**** | 5 | 2 | 6 | 10 | 3 |
| C H Field | 11 | 6* | n/a | 11 | 11 | 10 | n/a |
| J E Hall | 8 | 6* | 3* | 8 | 8 | 8 | 2 |
| P O Harrison *** | 4 | n/a | 2 | n/a | n/a | n/a | 1 |
| N J Holden | 10 | 7 | 5 | 11 | 11 | n/a | n/a |
| S A Howe | 11 | 3* | n/a | 10 | 11 | 10 | n/a |
| C F Plumbridge *** | 4 | 4* | n/a | 4 | 4 | n/a | n/a |
| J E Smith | 10 | 7 | 5 | 10 | 10 | 1 | 2 |
| N J Treble | 10 | 5 | 5 | 10 | 10 | 1 | 2 |
| C R L Wilson | 11 | 7 | 5 | 1 | 11 | 2 | n/a |

* Executive directors attended by invitation
** Management Committees attended by named Non-Executive Directors
*** Director retired at 2014 AGM
**** Attended on a voluntary basis

# DIRECTORS' REMUNERATION REPORT

(UNAUDITED)

The Board has an established Remuneration and Loans Committee which comprises all the Non-Executive Directors. It reviews and approves remuneration policy, packages and service contracts for Executive Directors and considers and approves loans to Directors or connected persons. This report explains how the Society voluntarily complies with the principles relating to remuneration in the UK Corporate Governance Code as well as meeting the requirements of the regulator's Remuneration Code.

## Remuneration and Loans Committee

The Committee is chaired by Jan Smith (Non-Executive Director, Vice Chairman and Senior Independent Director) and is responsible for recommending to the Board the overall remuneration policy and actual levels of remuneration for Executive Directors. The Committee also ensures compliance with the regulator's Remuneration Code. In reaching remuneration decisions the Committee reviews and takes into account benchmark data from the Building Societies Association (BSA) remuneration survey.

## Executive Directors' remuneration

The Board's policy is to set remuneration levels to attract and retain high quality Executive Directors. The Society operates in a competitive environment, from a sector as well as a geographic perspective. With the City of London within easy reach, sourcing and retaining high quality Executives is a key consideration. Performance at a high level is expected, with rewards directly linked to appropriate risk management, financial performance, quality customer service and individual excellence. Executive Directors are designated as "Code Staff" under the regulator's Remuneration Code due to their material impact on the Society risk profile.

The main components of the remuneration package for Executive Directors are:

## Basic salary

Basic salaries for Executive Directors take into account the following principal factors:

- Job content and responsibilities;
- Individual performance, assessed annually; and,
- Remuneration levels for similar positions in the financial services sector.

Executive Directors are not involved in deciding their own levels of remuneration.

In 2014, the basic salary of the Chief Executive remained at the 2013 level.

Payments are reflected in the remuneration table shown in Note 7.

There is an annual appraisal scheme for Executive Directors which incorporates 360 degree feedback. The results of this exercise help to inform salary awards.

## Bonus

In late 2013 the Remuneration Committee commissioned a review of our approach to rewarding all staff within the business. At its core was a desire to provide a framework where staff feel valued for excellent service provided to our Members and customers together with their overall contribution to the Society. We believe this level of recognition will encourage and motivate our staff to achieve, enabling existing staff retention and building on the attractiveness of Saffron as an employer for new talent. The review referenced market best practices, for example the John Lewis partnership model, with a desire to reflect a 'One Business' approach where all staff can contribute to, and are rewarded for, the success of the Society. The new scheme was introduced on the 1 August 2014.

For the period 1 January to 31 July 2014 the only scheme available to Code Staff was the Medium Term Incentive Plan (MTIP) scheme detailed below. The MTIP scheme was closed as at 31 July 2014 and replaced by the new 'One Business' bonus scheme framework. In the period to 31 July 2014 the Society's Executive Directors were eligible to accrue a medium term non-pensionable performance bonus under the terms of this MTIP. Medium term bonuses were capped at 30% of salary and only paid subject to achievement of core objectives on a deferred basis. Having achieved the objectives detailed in the 2014 operating plan in respect of gross profit, cost/income ratio, asset growth target, and capital adequacy requirements, customer satisfaction and personal contribution based on functional measure in the balance business scorecard, an accrual has been made. The scheme is now closed with any remaining bonus deferred payable in stages in each of 2015 and 2016.

For the period 1 August to 31 December 2014 and each year onwards the new 'One Business' scheme is available and detailed below.

There are 3 elements of the new scheme:
1. Our Contribution
2. My Contribution
3. Long-Term Performance (available to Code Staff)

Elements 1 and 2 are open to all Saffron permanent staff under the banner of the 'One Business' Scheme. Payments made under "Our" or "My" Contribution are not subject to deferral.

In practice

1. The Our Contribution element is based on achievement of both of Saffron's profit and customer objectives. The recognition of our staff's commitment to customer service and the relationship our Members have with the Society, is a significant enhancement to our approach in rewarding our staff. Achievement of this target is reflected in a payment of a flat rate sum, which is payable to all staff. The amount payable is dependent on the performance of the business and will be £0 to £1,500 per individual, regardless of position.
2. The My Contribution element is based on an individual's contribution against their agreed performance objectives. Performance against these objectives is reviewed via an individual's appraisal. Assuming that the individual's objectives have been fully met, the My Contribution bonus element is calculated on a percentage of basic salary from 5% to 20%, dependent on the appraisal rating.

# DIRECTORS' REMUNERATION REPORT

(UNAUDITED)

3. The Long-Term Performance element is open to Code staff. The scheme allows for a payment to be made of up to 20% of basic salary and only paid subject to achievement of core objectives on a deferred basis. Having achieved the objectives detailed in the 2014 operating plan, in respect of gross profit, cost/income ratio, asset growth target, customer satisfaction, capital adequacy requirements and personal contribution based on functional measures in the balance business scorecard, an accrual will be made. The deferral element is spread over 2 years with 50% payable in 2015 and 50% payable in 2017.

Bonuses paid in 2014 are shown in the table of remuneration in Note 7.

The Society bonus scheme is non-contractual and in relation to any long-term performance element the Remuneration Committee can decide at any time to withdraw or amend the terms on which it is based. This may include a mid-year review of performance targets if unforeseen circumstances come to light which undermine the integrity of, or intention behind the scheme. If the scheme is terminated for any reason the long-term performance bonus options already granted will continue to be exercisable in accordance with normal scheme rules until all entitlement to payment has been exhausted.

In the event of non-achievement of targets, by either the Society or an individual Director, the long-term performance element will not be accrued for that year and where it is considered appropriate may also result in the reduction of the bonus already vested from previous years but not yet paid. This will also be the case in the event of misstatement, misconduct and non-performance by an individual. It should be noted these measures are not expected to be used except in exceptional circumstances.

All payments under the bonus scheme are non-pensionable.

For the avoidance of doubt the regulator's Remuneration Code applies to all Executive Directors' remuneration and the scheme is designed to meet these requirements. In the event of any conflict between this scheme and the Code, the Code requirements will prevail.

## Pensions

The Executive Directors are included in the Society's Group Personal Pension Plan which offers benefits to staff irrespective of seniority. The current employer contribution for Directors is 13.5% of basic salary, unchanged from 2013.

## Other benefits

The Executives Directors are also eligible for a fully expensed Society car, permanent health insurance and private medical insurance. The Society has no share option scheme and none of the Executive Directors have any beneficial interest in, or any rights to subscribe for shares in any subsidiary undertaking. Executive Directors are not entitled to salaries or fees from subsidiary directorships. There is in existence a non-contractual redundancy payment scheme which could provide an enhanced redundancy payment of up to a maximum of 40 weeks salary. This scheme applies to all Executive Directors and staff and could be withdrawn without notice. Any payment would be at the sole discretion of the Board (in the case of Executive Directors) and if it exceeded the statutory redundancy entitlement, would be the only payment made. If it was not approved, then there would still be an entitlement to the statutory redundancy payment.

## Service contracts

All Executive Directors are employed on a permanent service contract. Details are included in the Annual Business Statement on page 44.

Non-Executive Directors are appointed by letter for a 3 year period and are generally expected to serve a second 3 year term. Appointment can be extended further up to a maximum of 3 years if the Non-Executive Director takes on a significant new role, for example that of Chairman or Vice Chairman during this period.

## Executive Directors' personal development

In order to facilitate the personal development of an Executive Director, it is Board policy that an Executive Director will be permitted to undertake a Non-Executive role with another non-competing organisation. Any Executive Director wishing to undertake such a role whilst employed by the Society will need in principle approval from the Chief Executive (or in the case of the Chief Executive, in principle approval from the Chairman). Full approval will be sought from the Nominations Committee following submission of a full proposal. Any fees derived from the Non-Executive role will be paid directly to the Society Community Fund. Executive Directors' will not benefit financially in any way from this arrangement.

## Non-Executive Directors' fees

The Remuneration and Loans Committee reviews the level of fees for Non-Executive Directors each year, taking into account data on fees paid in the mutual financial services sector, levels of responsibility, time commitments and the recommendations of the Chief Executive and the Chief People Officer. Recommendations are referred to the full Board for approval.

When reviewing fees payable to Non-Executive Directors for 2014, reference has been made to the increasing level of time commitment and complexity associated with the role as well as benchmarking among peer group Building Societies and other similar financial services sector organisations. As a result, fees for Non-Executive Directors were increased in 2014, having remained at a fixed level since 2011.

There are no bonus schemes or other deferred benefits for Non-Executive Directors and they are not entitled to any pension from the Group.

## Analysis of Directors' remuneration

The remuneration of each Director is analysed in Note 7 of the Report and Accounts.

This report is published with the aim of giving Members an insight into how the decisions around Directors' remuneration are taken. A resolution will be put forward at the Annual General Meeting inviting Members to vote on the report on Directors' remuneration. The vote is advisory and the Board will take into account Members' views in determining future policy.

# DIRECTORS' REPORT

The Directors submit their Report prepared in the context of the UK Corporate Governance Code and in accordance with the requirements of the Building Societies Act.

## Information presented in other sections

Certain information required to be included in a Director's report can be found in the other sections of the Annual Report and Accounts as described below. All of the information presented in these sections is incorporated by reference into this Directors' report and is deemed to form part of this report:

- Commentary on the Group's results for the year, assets and capital together with likely future developments in the business of the Group is included in the Chief Executive's Review;
- Commentary on the Group's principal risks and uncertainties is set out in the Business Model and Strategy;
- A description of the Group's financial risk management objectives and policies and its exposure to risks arising from its use of financial instruments set out in Note 25 to the Accounts; and,
- Information concerning Directors' contractual arrangements and entitlements is given in the Directors' Remuneration Report.

This includes information set out in the Chairman's Statement, Chief Executive's Review and Notes to the Accounts.

## Events since the year end

The Directors consider there has been no event since the end of the financial year which would have a significant effect on the position of the Group.

## Mortgage arrears

At Group level at 31 December 2014 there were no accounts (2013: nil) where payments were 12 months or more in arrears.

At 31 December 2014, the Group held 20 properties (2013: 21) in possession.

## Supplier payment policy

The Group will discharge suppliers' invoices within agreed terms when they fully conform to the terms and conditions of the purchase.

## Our people

Once a year the Board reviews employment policies and ensures that they are designed to provide fair and effective employment conditions and equal opportunities. The Society retains its commitment to the development of its staff and the alignment of individual goals to the Society's aims.

We would like to thank all our staff for the hard work and support they have given the Society over the last 12 months.

## Charitable donations

During the year the Society made donations totalling £12,804 (2013: £14,084) in support of charities and organisations. No contributions were made for political purposes (2013: nil).

## Business associates

We would like to thank our solicitors, auditor, agents and professional advisors for their continued support during the year.

## Directors

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

T J Bayley (Non-Executive Director. Retired at the Annual General Meeting on 29 April 2014 and did not stand for re-election)

G R Dunn (Non-Executive Director & Chairman from April 2014)

J E Hall (Chief Executive Officer, resigned 22 October 2014)

P O Harrison (Chairman. Retired at the Annual General Meeting on 29 April 2014 and did not stand for re-election)

C F Plumbridge (Finance Director, retired on 1 May 2014)

J E Smith (Vice Chairman and Senior Independent Director, Non-Executive Director)

C R L Wilson (Non-Executive Director)

T G Barr (Non-Executive Director)

N J Holden (Non-Executive Director)

N J Treble (Non-Executive Director)

S A Howe (Chief Customer Officer)

C H Field (Chief Financial Officer)

Being eligible C H Field, S A Howe, T G Barr, N J Holden, J E Smith and N J Treble will stand for election, and re-election.

Biographies of the Directors appear at pages 21 to 22.

None of the Directors hold any shares in, or debentures of, any associated body of the Society.

## Auditor

Deloitte LLP has acted for the Society throughout 2014 and has audited the Group accounts for 2014, which are published here.

A resolution to re-appoint Deloitte LLP as auditor to the Group will be proposed at the Annual General Meeting.

Geoffrey Dunn, Chairman
On behalf of the Board
5 March 2015

# DIRECTORS' RESPONSIBILITIES

The following statement should be read in conjunction with the statement of the Auditor's responsibilities in relation to the preparation of the Annual Accounts, Annual Business Statement and Directors' report.

The Directors are required by the Building Societies Act 1986 (the Act) to prepare, for each financial year, Annual Accounts which give a true and fair view of the:

- state of the affairs of the Society and the Group at the end of the financial year;
- income and expenditure of the Society and the Group for the financial year; and,
- details of Directors' emoluments in accordance with Part VIII of the Act and regulations made under it.

In preparing these accounts, the Directors are required to:

- select appropriate accounting policies and apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether the applicable UK accounting standards have been followed, subject to any material departures discussed and explained in the Accounts; and,
- prepare the Accounts on the going concern basis unless it is inappropriate to presume that the Group will continue in business.

In addition to the Accounts, the Act requires the Directors to prepare, for each financial year, an annual business statement and a Directors' report, each containing prescribed information relating to the business of the Society and its subsidiaries.

## DIRECTORS' RESPONSIBILITIES FOR ACCOUNTING RECORDS AND INTERNAL CONTROLS

The Directors are responsible for:

- ensuring the Society and subsidiary undertakings keep accounting records in accordance with the Act;
- taking reasonable care to establish, maintain, document and review such systems and controls as are appropriate to its business in accordance with the rules made by the Financial Conduct Authority under the Financial Services and Markets Act 2000; and,
- safeguarding the assets of the Group and for taking reasonable steps for the prevention and detection of fraud and other irregularities.

As well as our branch and agency network the Society operates a comprehensive website www.saffronbs.co.uk. The maintenance and integrity of this site is the responsibility of the Directors.

Legislation in the United Kingdom governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

# DIRECTORS' BIOGRAPHIES

The Board of the Saffron Building Society is made up of Executive and Non-Executive Directors. The role of the Executive Directors is to deal with the day-to-day running of the Society, while Non-Executive Directors, who are from a range of different specialist areas, bring an outside perspective to the management of the Society and also represent the views of the Membership. The following directors were in office as at 31 December 2014.

### Non-Executive Director – GARY BARR

Gary is an IT leader with over 25 years experience in industry including retail, manufacturing, health and services. As IT Director at the National Blood Service (NBS) he led the successful implementation of the award winning Pulse programme which created a single system for managing the blood supply in England, from donor to hospital. After leaving the NBS he joined Welcome Break, the Motorway Services provider, completely refreshing and replacing the business systems. He then went on to lead the IT team at Sodexo UK & Ireland running a variety of systems over 2000 sites. He started to work for WM Morrisons in 2006, as IT Director where he was key to the launching and leading of the Evolve programme, one of Europe's largest retail IT transformations. After leaving WM Morrisons he joined Dixons Group the electrical retailer as Group IT Director. In 2014 he decided that after 25 years in operational IT management it was time for a change and is pursuing a consulting and a non-executive career. He has also served as a Governor at Bedfordshire University and has sat on several industry advisory boards.

Gary joined the board in 2014 as a Non-Executive Director and sits on the Change Board; Remuneration and Loans; Risk, Audit, Compliance and Conduct Committees. Gary has lived in East Anglia for over 20 years and much of his free time is spent facilitating his daughter's passion for all things equestrian.

### Chairman – GEOFFREY DUNN

Geoffrey Dunn lives in Suffolk and has more than 40 years experience of financial management, mostly in financial services, and IT services. After graduating from Manchester Business School, he joined 3i plc and later worked in Corporate Finance at the merchant bank, S G Warburg and also GKN plc, before he joined Midland Bank and became Head of Finance & Planning for the International Division of the Bank. Subsequently, he became Group Finance Director of the global financial broker, Exco International plc. A move to Brussels followed as Chief Financial Officer (CFO) of SWIFT – the inter-bank messaging co-operative and network provider and later as CFO of the global telecoms operator, Global One. He returned to the UK as Group FD of Xansa, the FTSE listed IT company. In the last decade, Geoff has undertaken a number of major interim financial roles including: Finance Director of the Bank of England and also CFO of Northern Rock plc for the reconstruction and split of Northern Rock in 2009.

Geoff is also a Non-Executive Director and the Deputy Chairman of the Supervisory Council of Citadele Banka, based in Latvia. He is a Fellow of the Association of Corporate Treasurers. Geoff joined the Board in May 2011 and was appointed Chairman of the Society in May 2014.

### Chief Financial Officer – COLIN FIELD

Colin is a Chartered Accountant (FCA) and is currently Deputy President of his ICAEW District Society.

Colin was promoted to the role of Chief Financial Officer (CFO) and appointed to the Board in May 2014, having joined Saffron as Group Financial Controller in 2013. In his role of CFO, Colin chairs the Assets and Liabilities Committee (ALCO).

Prior to joining Saffron, Colin has had held a number of senior finance positions with Barclays, Caudwell Group and Willis Group having previously qualified with PriceWaterhouseCoopers.

### Non-Executive Director – NEIL HOLDEN

Neil Holden is a Chartered Accountant with 30 years experience in financial services. After qualifying with Thomson McLintock & Co (now KPMG) he held a number of executive roles in financial services mainly in financial control and risk management with JP Morgan, Hambros Bank, Westdeutsche Landesbank and Standard Bank Group, when he was Head of Risk for the International Operations and latterly Head of Credit for the worldwide corporate and investment banking business.

After leaving Standard Bank in 2006 Neil set up his own risk and governance advisory business consisting of several non-executive directorships together with advisory work for other clients. Neil is a Non-Executive Director of Bank of London and The Middle East plc (Chairman of Remuneration Committee), Integrated Financial Arrangements plc (Chairman of Audit Committee and Remuneration Committee) and Stanbic International Insurance Limited. He also advises financial services clients on risk and governance through Calmindon Limited.

As Chair of Saffron's RACCC Neil is using his skills and experience to foster and develop the solid foundation of assurance, governance and risk management that the Society and the previous Chairman has built, and is working with the executive team to ensure that this stays strong and relevant to Saffron's strategy, developing needs and regulatory obligations.

Neil joined the Board in April 2014. Neil has lived in North Essex for 25 years.

# DIRECTORS' BIOGRAPHIES

### Chief Customer Officer – SARAH HOWE

Sarah joined the Society as Chief Marketing Officer in March 2013. Sarah has over 25 years experience in a range of high profile marketing roles inside and outside financial services. Prior to joining the Society she was the Marketing Director for over 50s insurance intermediary brands RIAS and Castle Cover, both part of the Ageas Group. In this role she developed a multi-brand strategy and marketing integration plan following Ageas' purchase of Castle Cover Limited. Sarah also worked at Bupa for 11 years during which time she was appointed to the role of Chief Marketing Officer for the UK Insurance Division, leading the delivery of member focused product solutions, communication strategies and membership loyalty programmes. Sarah began her marketing career in the Home Shopping retail sector.

Sarah was appointed to the Board in May 2014. She lives in Essex.

### Non-Executive Director, Senior Independent Director & Vice Chairman – JAN SMITH

Jan Smith is a Strategy, Marketing and Customer Service Specialist. She has extensive experience with financial services organisations as Marketing and Sales Director with First Direct, Director of Retail Marketing with TSB Bank plc and Group Marketing and Sales Director for LV=. She was also Group Strategic Director for RAC plc and Sales and Marketing Director for Mazda Cars (UK) Limited. Since 1998 she has run her own London based marketing strategy company, working with clients such as The Open University, Co-operative Group, and Rosgosstrakh, the largest insurance company in Russia, among others.

Jan is a Non-Executive Director for the Council for Licensed Conveyancers where she also chairs the Remuneration Committee. She has held Non-Executive Director positions in a number of different organisations over the last 12 years including Royal Mint and HM Land Registry. These roles across industry sectors give her a broader perspective both on the running of a business and on the operation of the Board itself. Jan joined the Board in 2005 and has made a significant contribution as a champion for great service provision and with a passion to see the Society as the provider of choice for Members in the region. Jan chairs Remuneration & Loans Committee and is a member of Credit Committee and RACCC. She has been Senior Independent Director since 2011.

### Non-Executive Director – NICK TREBLE

Nick has 30 years experience in financial services, working primarily in the areas of treasury, capital markets, risk management, retail and commercial banking.

Most recently he was CEO of AIB Group (UK) plc, a retail and commercial bank operating in Great Britain as Allied Irish Bank GB and in Northern Ireland as First Trust Bank. Previously he was AIB plc Group Chief Risk Officer (2008) and Group Treasurer (2001 to 2008). From 1982 to 2001 he held a number of technical and managerial roles in treasury, asset & liability management, funding and trading for AIB plc. Nick retired from AIB in December 2012.

Nick joined the Board in April 2014 as a Non-Executive Director. In addition to the Board, he serves on the RACCC; Remuneration and Loans; Nominations; Assets and Liabilities; and the Credit Committee. He is married with 2 children and has lived near Cuffley, Hertfordshire for the last 17 years. He is a Member of the Association of Corporate Treasurers.

### Non-Executive Director – CHARLES WILSON

Charles Wilson is a retired Solicitor with broad experience of the financial services sector, having worked at Abbey and Nationwide over a period of 22 years. He headed the legal function at Abbey for 9 years before moving to Nationwide where he was a member of the executive management team with personal responsibility for legal and regulatory compliance and company secretarial. He also served on several industry bodies during this time, including the board of the Financial Ombudsman Service and the working group that established the LINK cash machine network. Since taking early retirement in 2005, Charles had one other Non-Executive directorship until 2008 with Hazell Carr plc, a company engaged in providing outsourcing support to the financial services and utilities sectors.

In addition to the Board, Charles serves on the Remuneration and Loans; and Credit Committee. Charles joined the Board in July 2009 as a Non-Executive Director.

# INDEPENDENT AUDITOR'S STATEMENT TO THE MEMBERS AND DEPOSITORS OF SAFFRON BUILDING SOCIETY

We have examined the summary financial statements for the year ended 31 December 2014 which comprise the Results for the year, Statement of Total Recognised Gaines and Losses, and the Financial position at the end of the year, together with the summary Director's report.

This report is made solely to the Society's Members, as a body, in accordance with the section 76(5) of the Building Societies Act 1986. Our work has been undertaken so that we might state to the company's members those matters we are required to state to them in an auditor's report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, for our audit report, or for the opinions we have formed.

## Respective responsibilities of directors and auditor

The Directors are responsible for preparing the Strategic Report (which includes the summary financial statements) and the supplementary material in accordance with applicable United Kingdom law.

Our responsibility is to report to you our opinion on the consistency of the summary financial statements contained within the Annual Member's Review with the full Annual Accounts, Annual Business Statement and Directors' report and its conformity with the relevant requirements of Section 76 of the Building Societies Act 1986 and regulations made under it.

We also read the other information contained in the Strategic Report and the supplementary material as described in the contents section, and consider the implications for our report if we become aware of any apparent misstatements or material inconsistencies with the summary financial statements.

We conducted our work in accordance with Bulletin 2008/3 issued by the Auditing Practices Board, "The auditor's statement on the summary financial statement in the United Kingdom" issued by the Auditing Practices Board" Our report on the Group and Society's full annual financial statements describes the basis of our opinion on those financial statements, the Strategic Report and the Directors' Report.

## Opinion

In our opinion, the summary financial statements are consistent with the full Annual Accounts, the Annual Business Statement and Director's Report of Saffron Building Society for the year ended 31 December 2014 and complies with the applicable requirements of Section 76 of the Building Societies Act 1986 and regulations made under it.

**Deloitte LLP**

Chartered Accountants and Statutory Auditors
Birmingham, United Kingdom
5 March 2015

# THE ACCOUNTS

## Income and expenditure account

for the year ended 31 December 2014

| | Notes | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|---|
| Interest receivable and similar income | 2 | 35,274 | 34,528 | 35,299 | 34,513 |
| Interest payable and similar charges | 3 | (17,324) | (17,324) | (21,185) | (21,185) |
| Net interest receivable | | 17,950 | 17,204 | 14,114 | 13,328 |
| Pension finance income | 8 | 167 | 167 | 109 | 109 |
| Income from investments | | – | 400 | – | 300 |
| Fees and commissions receivable | | 3,245 | 3,269 | 3,191 | 3,219 |
| Fees and commissions payable | | (1,749) | (1,747) | (1,486) | (1,478) |
| Other operating income | | 176 | 161 | 185 | 171 |
| Total income | | 19,789 | 19,454 | 16,113 | 15,649 |
| Administrative expenses | 5 | (12,742) | (12,712) | (11,090) | (11,059) |
| Depreciation | | (1,273) | (1,273) | (871) | (871) |
| Other operating charges | 4 | – | – | (3) | (3) |
| Operating profit before provisions | | 5,774 | 5,469 | 4,149 | 3,716 |
| Provisions for bad and doubtful debts | 9 | (1,232) | (1,152) | (399) | (349) |
| Provisions for liabilities and FSCS Levy | 24 | (761) | (761) | (699) | (699) |
| Operating profit after provisions | | 3,781 | 3,556 | 3,051 | 2,668 |
| Net profit on disposal of operations | 13 | – | – | 68 | – |
| Operating profit on ordinary activities before tax | | 3,781 | 3,556 | 3,119 | 2,668 |
| Tax on profit on ordinary activities | 10 | (830) | (695) | (799) | (624) |
| Profit for the financial year | 22 | 2,951 | 2,861 | 2,320 | 2,044 |

All results were derived from continuing operations.

## Statement of total recognised gains and losses

for the year ended 31 December 2014

| | Notes | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|---|
| Profit for the financial year | | 2,951 | 2,861 | 2,320 | 2,044 |
| Actuarial (loss) recognised in the pension scheme | 8 | (877) | (877) | (129) | (129) |
| Movement in deferred tax relating to the pension scheme | 8 | 175 | 175 | 43 | 43 |
| Unrealised (loss) on revaluation of fixed assets | 23 | – | – | (319) | (319) |
| **Total gains and losses recognised since last Annual Accounts** | | 2,249 | 2,159 | 1,915 | 1,639 |

The notes on pages 27 to 42 form part of these accounts.

# Balance sheet

for the year ended 31 December 2014

| **Assets** | Notes | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|---|
| Liquid assets | | | | | |
| Cash in hand and balances with the Bank of England | | 870 | 660 | 676 | 639 |
| Loans and advances to credit institutions | 11 | 55,507 | 55,507 | 57,751 | 57,751 |
| Debt securities | 11 | 197,911 | 197,911 | 270,526 | 270,526 |
| | | 254,288 | 254,078 | 328,953 | 328,916 |
| Loans and advances to customers | | | | | |
| Loans fully secured on residential property | 12 | 896,453 | 851,709 | 838,401 | 791,144 |
| Other loans | 12 | 3,474 | 3,474 | 5,355 | 5,355 |
| | | 899,927 | 855,183 | 843,756 | 796,499 |
| Investments in subsidiary undertakings | 13 | – | 43,343 | – | 45,812 |
| Tangible fixed assets | 14 | 14,308 | 14,308 | 12,015 | 12,015 |
| Other assets | 15 | 152 | 31 | 1,142 | 1,041 |
| Prepayments & accrued income | | 1,483 | 1,483 | 690 | 690 |
| Net pension asset | 8 | 366 | 366 | 982 | 982 |
| **Total assets** | | 1,170,524 | 1,168,792 | 1,187,538 | 1,185,955 |
| **Liabilities** | | | | | |
| Shares | 16 | 952,228 | 952,228 | 915,829 | 915,829 |
| Amounts owed to credit institutions | 17 | 18,650 | 18,650 | 22,742 | 22,742 |
| Amounts owed to other customers | 18 | 139,149 | 139,149 | 190,152 | 190,152 |
| | | 1,110,027 | 1,110,027 | 1,128,723 | 1,128,723 |
| Other liabilities | 19 | 1,667 | 1,547 | 2,212 | 2,152 |
| Accruals and deferred income | 20 | 1,727 | 1,696 | 1,749 | 1,718 |
| Subordinated liabilities | 21 | 10,000 | 10,000 | 10,000 | 10,000 |
| | | 1,123,421 | 1,123,270 | 1,142,684 | 1,142,593 |
| General reserves | 22 | 46,324 | 44,743 | 44,026 | 42,534 |
| Revaluation Reserve | 23 | 779 | 779 | 828 | 828 |
| **Total liabilities** | | 1,170,524 | 1,168,792 | 1,187,538 | 1,185,955 |

The notes on pages 27 to 42 form part of these accounts.

These accounts were approved by the Board of Directors on 5 March 2015 and were signed on its behalf by:

G R Dunn
Chairman

C H Field
Chief Financial Officer

M T Kirsch
Interim Chief Executive

# Group cashflow statement

for the year ended 31 December 2014

| | Group 2014 £000 | Group 2013 £000 |
|---|---|---|
| **Net cash (outflow) / inflow from operating activities (see below)** | (83,663) | 4,693 |
| Tax paid | (631) | (444) |
| Tax Received | 22 | – |
| **Capital expenditure and financial investment** | | |
| Net sale of debt securities | 71,825 | 14,077 |
| Purchase of tangible fixed assets | (3,566) | (4,770) |
| Net cash inflow from sales of fixed assets | – | – |
| **(Decrease) / Increase in Cash** | (16,013) | 13,556 |
| **Reconciliation of operating profit to net cash inflow / (outflow) from operating activities** | | |
| Operating profit | 3,781 | 3,119 |
| Decrease / (Increase) in prepayments and accrued income | 747 | (1,476) |
| (Decrease) / Increase in accruals and deferred income | (698) | 1,092 |
| Increase in provisions for bad and doubtful debts | 1,048 | 343 |
| Depreciation and amortisation | 1,273 | 871 |
| Pension contributions | – | (560) |
| Pension charges | (100) | (34) |
| **Net cash inflow from trading activities** | 6,051 | 3,355 |
| (Increase) in loans and advances to customers | (57,221) | (8,811) |
| Increase / (Decrease) in shares | 37,209 | (6,189) |
| (Decrease) in amounts owed to credit institutions | (4,119) | (32,338) |
| (Decrease) / Increase in amounts owed to other customers | (51,112) | 16,070 |
| (Increase) / Decrease in loans and advances to credit institutions | (13,959) | 33,348 |
| (Decrease) in other liabilities | (512) | (742) |
| **Net cash (outflow) / inflow from operating activities** | (83,663) | 4,693 |

| **Analysis of increase in cash** | 2013 Cash Balances £000 | Net Increase £000 | 2014 Cash Balances £000 |
|---|---|---|---|
| Cash in hand | 676 | 194 | 870 |
| Loans and advances to credit institutions repayable on demand (Note 11) | 44,280 | (16,207) | 28,073 |
| | 44,956 | (16,013) | 28,943 |

The Society has taken advantage of the exemption in FRS1, "Cash Flow Statements", which provides that where a company is a member of a group and a Consolidated Cash Flow Statement is published, the Society does not have to prepare a Cash Flow Statement.

# Notes to the accounts

## 1. Accounting policies

### a) Basis of preparation:

The accounts have been prepared under the historical cost convention, modified to include revaluations of certain fixed assets, and in accordance with applicable United Kingdom accounting standards, the Building Societies (Accounts and Related Provisions) Regulations 1998 and the relevant aspects of the Statements of Recommended Practice issued by the British Bankers' Association and regarded as best practice for the industry.

As noted in the Business Review, the Directors are satisfied that the Group has adequate resources to continue in business for the foreseeable future. For this reason the accounts continue to be prepared on the going concern basis.

Included in other creditors is the FSCS levy of £413,500 which is the expected interest charge for scheme year April 2014 to March 2015. The Group adopted in 2013 IFRIC 21 'Levies' which led to a change in the trigger for recognition at that point.

The contingent aspect of the levy is described in Note 24.

### b) Basis of consolidation:

The Group accounts consolidate the accounts of the Society and its subsidiary undertakings. In the Society accounts, investments in the subsidiary undertakings are stated at cost less impairment.

### c) Liquid assets:

Debt securities intended for use on a continuing basis in the Society's activities are classified as financial fixed assets and are stated at cost. Premiums and discounts arising on the purchase of financial fixed assets are amortised over the period to maturity of the security. Any amounts so amortised are charged or credited to the Income and Expenditure Account for the relevant financial years. Other liquid assets are stated at the lower of cost or net realisable value.

### d) Taxation:

Corporation tax is charged on profits adjusted for tax purposes. Deferred tax is provided for without discounting on timing differences arising from the allocation of certain income and expenditure to different periods for tax and accounts purposes, except as otherwise required by FRS19.

### e) Fixed assets and depreciation:

Freehold properties comprise branches and office buildings, and are stated at revalued amounts, being the fair value, determined by market based evidence, at the date of the valuation less any subsequent accumulated depreciation and subsequent impairment. Full valuations are completed every five years followed by interim valuations three years later. The Directors review the valuations to confirm that they remain appropriate in the intervening years. Increases in valuations of freehold buildings are credited to the revaluation reserve except where they reverse decreases for the same assets previously recognised in the income and expenditure account, in which case the increase in the valuation is recognised in the Income and Expenditure Account. Decreases in valuations are recognised in the Income and Expenditure Account except where they reverse amounts previously credited to the revaluation reserve for the same asset, in which case the decrease in valuation is recognised in the revaluation reserve.

Assets are depreciated over their estimated useful lives as follows:

- Freehold premises – 50 years
- Short leasehold premises – over the remainder of the lease
- Computer equipment and related software – 4-7 years
- Production software – 7 years
- Motor vehicles – 6 years
- Other equipment, fixtures and fittings – 10 years

### f) Premiums on the acquisition of mortgages:

Premiums arising on the acquisition of mortgage portfolios are amortised over five years, or the economic life of the portfolio if shorter, the amount amortised being included within other charges. Unamortised premiums are included within other assets in the Balance Sheet.

### g) Retirement benefits:

The Society operates a final salary pension scheme administered by trustees, the funds of which are separate from those of the Society. The defined benefit scheme is funded by contributions partly from the employees and partly from the Society at rates assessed by independent actuaries.

The scheme assets are measured at market value at each Balance Sheet date and liabilities are measured using the projected unit valuation method, discounted using a corporate bond rate. The resulting pension scheme surplus or deficit is recognised immediately on the Balance Sheet, net of deferred tax, and any resulting actuarial gains and losses are recognised immediately in the Statement of Total Recognised Gains and Losses.

The Society also operates a stakeholder pension scheme and the Society contributions for this scheme are charged to the Income and Expenditure Account.

### h) Provision for bad and doubtful debts:

Provisions are made to reduce the value of loans and advances to the amount which the Directors consider is likely to be recoverable.

Specific provisions are made against loans and advances when, in the opinion of the Directors, it is considered likely that losses may ultimately be realised. Currently this is considered to be where arrears are more than two months behind and exceed 2.5% of the outstanding loan balance. Anticipated losses on these accounts are calculated as the difference between the achievable market value of the security, calculated by applying an industry recognised house price index less forced sale deduction to valuations, and the outstanding loan balance, after making appropriate allowance for costs of repossession and sale. A factor is then applied to the provision based on the loan's recent performance. Allowance is made for loss insurance cover where appropriate.

A general provision is made to cover latent losses which, although not specifically identified, are known from experience to exist in the Group's loan portfolios. Such provisions are calculated using a combination of past loss experience, lending quality and consistency with industry levels. An additional provision is also made to cover Buy-To-Let properties which are on a forbearance

# Notes to the accounts (continued)

strategy. These provisions are regularly reviewed against actual experience.

For equity release mortgages, within general provisions, a provision for expected loss using estimated mortality rates and future house price estimates is recognised and is reviewed annually.

The Group uses forbearance measures to assist borrowers who have difficulties in meeting their obligations, as set out in Note 12. Where the Group considers that a loss may arise in these cases, provisions are made in accordance with the policy noted above.

### i) Mortgage discounts and other incentives:

Cash incentives and other expense related incentives to borrowers are included in 'Other operating charges' when paid. Fee income is also recognised when paid with the exception of material arrangement fees where income is spread over the period of discount or fixed rate. Interest discounts reduce interest receivable over the period of the discount.

### j) Hedging rate and instruments:

All interest rate hedges are held off-Balance Sheet and are valued on an equivalent basis to the underlying asset. Cashflows arising in relation to such instruments are accounted for on an accruals basis. If the hedge contract is terminated early, the realised gain or loss is recognised immediately to the Income and Expenditure Account.

If the underlying instrument is redeemed, the remaining unamortised amount is immediately charged/credited to the income and expenditure account. Amounts accrued on hedging contracts and instruments are included within 'Other assets' or 'Other liabilities'.

### k) Operating leases:

Rentals under operating leases are charged to administrative expenses in the income and expenditure account on a straight line basis over the life of the lease.

### l) Interest income recognition:

All of the Society's material sources of income including interest receivable, fees and commissions receivable, and interest income in respect of all loans is credited to the Income and Expenditure Account as it becomes receivable. Application and completion fees charged to mortgage customers relating to the cost of processing the application are recognised in the period in which they are charged. Where a fee is regarded as including an element of ongoing processing costs, that element of the fee is spread over the period to which it applies. Valuation and other fees receivable from mortgage applicants and fees payable to third parties are included in the accounts in the period to which they relate within fees and commissions receivable and fees and commissions payable respectively.

# Notes to the accounts (continued)

## 2. Interest receivable and similar income

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| On loans fully secured on residential property | 36,663 | 34,302 | 35,416 | 32,952 |
| On loans to subsidiaries | – | 1,615 | – | 1,678 |
| On other loans | 232 | 232 | 320 | 320 |
| On debt securities<br>Interest from fixed income securities | 285 | 285 | 90 | 90 |
| On other liquid assets<br>Interest and other income | 1,621 | 1,621 | 1,886 | 1,886 |
| Gains arising on the disposal of financial instruments | 1 | 1 | 719 | 719 |
| Net expense on financial instruments | (3,528) | (3,528) | (3,132) | (3,132) |
| | 35,274 | 34,528 | 35,299 | 34,513 |

There were no significant gains arising on the disposal of financial instruments which were previously held for hedging purposes (2013: £724,000).

## 3. Interest payable and similar charges

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| On shares held by individuals | 14,566 | 14,566 | 17,363 | 17,363 |
| Subordinated liabilities | 632 | 632 | 632 | 632 |
| Net expense on Financial Instruments | 466 | 466 | 129 | 129 |
| Other | 1,660 | 1,660 | 3,061 | 3,061 |
| | 17,324 | 17,324 | 21,185 | 21,185 |

## 4. Other operating charges

Other operating charges comprise cash incentives, legal fees and amortisation of the premium arising from the purchase of mortgage books by Crocus Home Loans Limited.

## 5. Administrative expenses

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Staff costs (Note 6) | 6,734 | 6,734 | 5,672 | 5,672 |
| Remuneration of auditors:<br>statutory audit services | 49 | 49 | 62 | 62 |
| audit of the Company's subsidiaries pursuant to legislation | 6 | 6 | 7 | 7 |
| all other services | 37 | 37 | 127 | 127 |
| Operating lease rentals | 435 | 435 | 206 | 206 |
| Other administrative expenses | 5,481 | 5,451 | 5,016 | 4,985 |
| | 12,742 | 12,712 | 11,090 | 11,059 |

Note: all audit fees are borne by the Society.

# Notes to the accounts (continued)

## 6. Staff numbers and costs

| The average number of persons employed by the Society (including the Executive Directors) during the year was: | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Principal office | 107 | 107 | 101 | 101 |
| Branch offices | 62 | 62 | 64 | 64 |
| | 169 | 169 | 165 | 165 |

| The aggregate costs of these persons were as follows: | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Wages and salaries | 5,837 | 5,837 | 4,880 | 4,880 |
| Social security costs | 502 | 502 | 466 | 466 |
| Other pension costs (Note 8) | 395 | 395 | 326 | 326 |
| | 6,734 | 6,734 | 5,672 | 5,672 |

## 7. Remuneration of and transactions with directors

Analysis of Directors' emoluments:

| Executive | Salary/ fees £000 | Medium term bonus paid £000 | Other non– cash benefits £000 | Pension contributions £000 | Compensation for loss of office £000 | 2014 Total £000 | 2013 Total £000 |
|---|---|---|---|---|---|---|---|
| J E Hall (to 23.10.14) | 175 | 108 | 19 | 24 | – | 326 | 323 |
| C F Plumbridge (to 01.05.14) | 64 | 28 | 6 | 9 | 55 | 162 | 198 |
| S A Howe (from 01.05.14) | 97 | – | 8 | 13 | – | 118 | – |
| C H Field (from 01.05.14) | 100 | – | 10 | 12 | – | 122 | – |
| | 436 | 136 | 43 | 58 | 55 | 728 | 521 |
| **Non-Executive** | | | | | | | |
| P O Harrison (to 30.04.14) | 13 | – | – | – | – | 13 | 37 |
| T J Bayley (to 30.04.14) | 9 | – | – | – | – | 9 | 26 |
| G R Dunn | 40 | – | – | – | – | 40 | 22 |
| J E Smith | 35 | – | – | – | – | 35 | 26 |
| C R L Wilson | 28 | – | – | – | – | 28 | 22 |
| T G Barr (from 10.04.14) | 22 | – | – | – | – | 22 | – |
| N J Treble (from 27.03.14) | 23 | – | – | – | – | 23 | – |
| N J Holden (from 27.03.14) | 29 | – | – | – | – | 29 | – |
| | 199 | – | – | – | – | 199 | 133 |
| Total 2014 | 635 | 136 | 43 | 58 | 55 | 927 | – |
| Total 2013 | 496 | 73 | 38 | 47 | – | – | 654 |

Medium term bonus was earned and accrued between 2011 and 2013 with payment being deferred until 2014 to 2016. The bonus arrangements for Executive Directors are explained in full in the Directors' Remuneration Report.

Included in J E Hall's bonus is a deferred consideration of £45,000 payable in 2015 depending on post-employment conditions being met.

The Interim Chief Executive Officer, M T Kirsch, was paid £66,000 (including VAT) for his services from 10/11/14 to 31/12/14.

At 31 December 2014, there were no outstanding mortgage loans granted in the ordinary course of business to Directors and their connected persons (2013: £589,650). Details of these transactions are included in the Society's register of Directors' loans, extracted details of which are available for inspection by members during normal office hours at the Society's principal office for a period of 15 days prior to and including the Annual General Meeting.

# Notes to the accounts (continued)

## 8. Group pensions

### Defined contribution scheme

The amounts charged to the Income and Expenditure Account in respect of contributions to the Group's defined contribution stakeholder pension scheme represents the contribution payable in the year. The amounts paid into the scheme amounted to £395,000 (2013: £326,000).

### Defined benefit scheme

The Society operates a defined benefit pension scheme covering its longer serving employees. The scheme closed to staff who joined the Society after 4 August 2003 and closed to future accrual from 1 January 2008. Members who remain employed by the Society retain a link to pensionable salary. The assets of the scheme are held in a managed fund independent of the Society's finances.

The funding of the scheme is based upon regular triennial actuarial valuations, the most recent being as at 30 April 2014. The principal assumptions relate to the rate of return on investments, then assumed to be 5.4% (2011: 5.8%) per annum for the pre-retirement period and 4.0% (2011: 5.1%) for the post-retirement period. The rate of increase in salaries was assumed to be 3.6% (2011: 4.0%) per annum.

The scheme is shown in the Balance Sheet as a net pension asset, and is made up of the scheme's surplus of £458,000 (2013: £1,235,000) less the related deferred tax liability of £92,000 (2013: £253,000).

Based on an actuarial valuation, consistent with the methods prescribed in the standard, a net surplus on the Society scheme has been identified as follows:

| Date of Fund Valuation | 31 December 2014 | 31 December 2013 | 31 December 2012 | 31 December 2011 |
|---|---|---|---|---|
| **Main assumptions** | | | | |
| Rate of increase in salaries | 2.1% | 2.5% | 2.4% | 3.2% |
| Rate of increase in pensions in payment | 3.0% | 3.4% | 3.0% | 3.1% |
| Rate of increase in pensions in payment after 05.04.05 | 2.3% | 2.4% | 2.3% | 2.3% |
| Discount rate | 3.6% | 4.5% | 4.5% | 5.0% |
| RPI inflation assumptions | 3.1% | 3.5% | 3.1% | 3.2% |
| CPI inflation assumptions | 2.1% | 2.5% | 2.4% | 2.2% |

These assumptions used by the actuary are the best estimates, chosen from a range of possible assumptions which may not be borne out in practice.

The assets in the Scheme and the expected rates of return were:

| | Long term rate of return expected at 31 December 2014 | Value 31 December 2014 | Long term rate of return expected at 31 December 2013 | Value 31 December 2013 | Long term rate of return expected at 31 December 2012 | Value 31 December 2012 | Long term rate of return expected at 31 December 2011 | Value 31 December 2011 |
|---|---|---|---|---|---|---|---|---|
| Equities | 7.5% | 4,880 | 7.8% | 3,391 | 7.7% | 2,730 | 7.7% | 2,405 |
| Bonds | 3.4% | 6,569 | 4.4% | 5,553 | 4.1% | 5,750 | 4.7% | 5,171 |
| Property | 6.0% | – | 6.3% | 908 | 6.2% | 828 | 7.7% | 807 |
| Cash | 1.7% | 35 | 3.0% | 574 | 1.8% | 18 | 2.0% | 10 |
| Total market value of assets | | 11,484 | | 10,426 | | 9,326 | | 8,393 |
| Present value of scheme liabilities | | (11,026) | | (9,191) | | (8,556) | | (7,720) |
| Surplus in scheme | | 458 | | 1,235 | | 770 | | 673 |

The scheme liabilities were valued in accordance with the guidelines set out in FRS 17 using a discount rate of 3.6% per annum, which is derived from the yields available on high quality sterling corporate bonds at durations appropriate to the duration of liabilities.

| **Demographic assumptions** | **31 Dec 2014** | **31 Dec 2013** | **31 Dec 2012** | **31 Dec 2011** |
|---|---|---|---|---|
| Mortality (Pre retirement) | Nil deaths | AMC00/AFC00 | AMC00/AFC00 | AMC00/AFC00 |
| Mortality (Post retirement) | S2PAcmi | S1PAcmi | S1PAcmi | S1PAcmi |

# Notes to the accounts (continued)

## 8. Group pensions (continued)

| Movement in surplus during the year | 2014 £000 | 2013 £000 | 2012 £000 | 2011 £000 |
|---|---|---|---|---|
| Surplus at the beginning of year | 1,235 | 770 | 673 | 951 |
| Current service costs | (67) | (75) | (35) | – |
| Contributions | – | 560 | – | 250 |
| Pension finance income | 167 | 109 | 102 | 124 |
| Actuarial gain / (loss) | (877) | (129) | 30 | (652) |
| Surplus at the end of the year | 458 | 1,235 | 770 | 673 |
| Related deferred tax (liability) | (92) | (253) | (177) | (168) |
| Net pension asset | 366 | 982 | 593 | 505 |

**Analysis of other pension costs charged in arriving at operating profit:**

| | 2014 £000 | 2013 £000 |
|---|---|---|
| **Analysis of amounts included in other operating charges** | | |
| Current service cost | (67) | (75) |
| Net costs charged to other operating charges | (67) | (75) |
| **Analysis of amounts included in pension finance income** | | |
| Expected return on pension scheme assets | 579 | 494 |
| Interest on pension scheme liabilities | (412) | (385) |
| Net credit to other operating income | 167 | 109 |
| **Analysis of amount recognised in the statement of total recognised gains & losses** | | |
| Actual return less expected return on scheme assets | 605 | 199 |
| Experience gains and losses arising on scheme liabilities | (282) | – |
| Changes in assumptions underlying the present value of scheme liabilities | (1,200) | (328) |
| Total actuarial (loss) recognised in the statement of total recognised gains and losses | (877) | (129) |

**History of experience gains and losses**

| | 2014 £000 | 2013 £000 | 2012 £000 | 2011 £000 | 2010 £000 |
|---|---|---|---|---|---|
| Difference between the actual and expected return on assets | | | | | |
| £000 | 605 | 199 | 537 | (243) | 261 |
| percentage of scheme assets | 5.27% | 1.91% | 5.76% | 2.90% | 3.26% |
| Experience gains and losses | | | | | |
| £000 | (282) | – | 330 | (105) | – |
| percentage of scheme liabilities | 2.56% | 0.00% | 3.84% | 1.36% | 0.00% |
| Total actuarial gain or loss | | | | | |
| £000 | (877) | (129) | 30 | (652) | 373 |
| percentage of scheme liabilities | 7.95% | 1.40% | 0.35% | 8.45% | 5.30% |

# Notes to the accounts (continued)

## 9. Provision for bad and doubtful debts

Provisions against loans to customers have been made as follows:

| Group | Loans fully secured on residential property | | Other loans fully secured on land | | Total provisions for bad and doubtful debts | | |
|---|---|---|---|---|---|---|---|
| | Specific £000 | General £000 | Specific £000 | General £000 | Specific £000 | General £000 | Total Provision £000 |
| At 1 January 2014 | 573 | 2,417 | – | – | 573 | 2,417 | 2,990 |
| Charge / (credit) for the year | (214) | 1,446 | – | – | (214) | 1,446 | 1,232 |
| Amounts transferred in the period | 1,324 | (1,324) | – | – | 1,324 | (1,324) | – |
| Amounts utilised in the period | – | (184) | – | – | – | (184) | (184) |
| At 31 December 2014 | 1,683 | 2,355 | – | – | 1,683 | 2,355 | 4,038 |
| **Society** | | | | | | | |
| At 1 January 2014 | 568 | 1,883 | – | – | 568 | 1,883 | 2,451 |
| Charge / (credit) for the year | (224) | 1,376 | – | – | (224) | 1,376 | 1,152 |
| Amounts transferred in the period | 1,324 | (1,324) | – | – | 1,324 | (1,324) | – |
| Amounts utilised in the period | – | (176) | – | – | – | (176) | (176) |
| At 31 December 2014 | 1,668 | 1,759 | – | – | 1,668 | 1,759 | 3,427 |

## 10. Taxation on profit on ordinary activities

| The taxation charge for year comprises: | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Current tax charge | 576 | 422 | 826 | 667 |
| Deferred tax – origination and reversal of timing differences | 254 | 273 | (27) | (43) |
| Total tax charge | 830 | 695 | 799 | 624 |
| Factors affecting the tax charge for the year are: | | | | |
| Operating profit and profit on ordinary activities before tax | 3,781 | 3,556 | 3,119 | 2,668 |
| Profit on ordinary activities multiplied by 21.49% (2013: 23.25%) | 813 | 764 | 725 | 620 |
| Effects of: | | | | |
| Difference between capital allowances and depreciation | (145) | (145) | (60) | (60) |
| Other short term timing differences | (11) | (26) | 71 | 87 |
| Income not taxable for tax purposes | – | (86) | – | (70) |
| Disallowable expenses | 41 | 41 | 245 | 245 |
| Marginal Relief | – | – | – | – |
| Pension movements | (16) | (16) | (138) | (138) |
| Prior period adjustments | (106) | (110) | (17) | (17) |
| Current tax charge for the year | 576 | 422 | 826 | 667 |

The standard rate of Corporation Tax was 23% up to 31 March 2014 and 21% with effect from 1 April 2014, giving an effective rate for the year of 21.49%. In July 2013, a reduction in the corporation tax rate to 20% from 1 April 2015 was substantively enacted into legislation. All deferred tax balances have been recognised at 20%, being the rate enacted at the balance sheet date at which the balances are expected to reverse.

# Notes to the accounts (continued)

## 11. Liquid assets

Loans and advances to credit institutions repayable from the Balance Sheet date in the ordinary course of business are as follows:

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Accrued interest | 11 | 11 | 7 | 7 |
| On demand | 28,073 | 28,073 | 44,280 | 44,280 |
| In not more than three months | – | – | – | – |
| In more than three months but not more than one year | 27,423 | 27,423 | 13,464 | 13,464 |
| | 55,507 | 55,507 | 57,751 | 57,751 |
| Debt securities (unlisted) | | | | |
| Issued by public bodies | 22,289 | 22,289 | 41,869 | 41,869 |
| Issued by other borrowers | 175,622 | 175,622 | 228,657 | 228,657 |
| | 197,911 | 197,911 | 270,526 | 270,526 |
| Debt securities have remaining maturities as follows: | | | | |
| Accrued interest | 479 | 479 | 1,269 | 1,269 |
| In not more than one year | 121,966 | 121,966 | 206,161 | 206,161 |
| In more than one year | 75,466 | 75,466 | 63,096 | 63,096 |
| | 197,911 | 197,911 | 270,526 | 270,526 |

The unamortised premium on debt securities included above was £1,718,147 (2013: £3,152,154)

The Directors of the Society consider that the primary purpose of holding securities is prudential. Securities held as liquid assets are held with the intention of use on a continuing basis in the Society's activities and are classed as financial fixed assets.

Movements during the year of debt securities held as financial fixed assets, excluding accrued interest of £478,800 (2013: £1,269,000) are analysed as follows:

| Cost and Net book value | Group 2014 £000 |
|---|---|
| At 1 January | 269,257 |
| Additions | 329,396 |
| Disposals | (401,221) |
| At 31 December | 197,432 |

## 12. Loans and advances to customers

The remaining maturity of loans and advances to customers from the balance sheet date is as follows:

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| On call and at short notice | – | – | 3,581 | 3,540 |
| In not more than three months | 9,887 | 9,552 | 4,577 | 4,246 |
| In more than three months but not more than one year | 25,039 | 24,359 | 26,299 | 25,672 |
| In more than one year but not more than five years | 55,822 | 52,704 | 57,286 | 54,897 |
| In more than five years | 813,217 | 771,995 | 755,003 | 710,595 |
| | 903,965 | 858,610 | 846,746 | 798,950 |
| Less provision (Note 9) | (4,038) | (3,427) | (2,990) | (2,451) |
| | 899,927 | 855,183 | 843,756 | 796,499 |
| The maturity analysis comprises: Loans fully secured on residential property | 896,453 | 851,709 | 838,401 | 791,144 |
| Other loans - loans fully secured on land | 3,474 | 3,474 | 5,355 | 5,355 |
| | 899,927 | 855,183 | 843,756 | 796,499 |

# Notes to the accounts (continued)

### 12. Loans and advances to customers (continued)

Forbearance is where the Group enters into an arrangement with a borrower(s) when they have financial or other difficulties in meeting their obligations under the terms of their mortgage.

Where appropriate for customers' needs, the Group applies a policy of forbearance and may grant a concession to borrowers. This may be applied where actual or apparent financial stress of the customer is deemed short term with a potential to be recovered.

The Group will always try to work with borrowers to achieve the best outcome for both parties in these circumstances and to this end its policy on forbearance has three basic principles:

- the borrower's best interests and establishing a payment plan with the borrower which is practical in the terms of the borrower's circumstances and their ability to pay but which meets the needs of both parties;
- that the Group will continue to work with the borrower to bring the mortgage back onto sustainable terms within a time frame appropriate to their circumstances; and
- the Group will only initiate repossession proceedings when all other reasonable attempts to resolve the problem have failed.

The principal forbearance tools used are interest-only concessions and arrangements to repay arrears over a period which is practical in terms of the circumstances of the borrower. The majority of borrowers who require assistance are aided by one or other of these methods. The table below gives details of the loans subject to interest-only concessions and arrangements at 31 December 2014.

| | Interest only | | Arrangements | |
|---|---|---|---|---|
| **2014** | Account balances £000 | Number of accounts | Account balances £000 | Number of accounts |
| Society | 3,763 | 24 | 5,290 | 33 |
| Crocus | 252 | 4 | 1,159 | 11 |
| Group total | 4,015 | 28 | 6,449 | 44 |

| | Interest only | | Arrangements | |
|---|---|---|---|---|
| **2013** | Account balances £000 | Number of accounts | Account balances £000 | Number of accounts |
| Society | 8,457 | 54 | 4,072 | 33 |
| Crocus | 406 | 5 | 1,835 | 17 |
| Group total | 8,863 | 59 | 5,907 | 50 |

Other forbearance measures offered by the Group include a change to the date of payment each month, payment holidays, permanent change to mortgage type, mortgage term extensions and capitalisation of mortgage arrears.

Capitalisation of mortgage arrears is only offered where all other forbearance options have been exhausted and only when it is the right option for the customer. The Group policy, after obtaining the customers consent, is to capitalise arrears once the customer has made at least six consecutive contractual monthly mortgage repayments following the instance of non-payment. During 2014 no customer arrears were capitalised (2013: none).

Payment holidays – four were approved during 2014 (2013: one).

Mortgage term extensions – of the 49 (2013: 9) mortgage accounts that have had a term extension during the year all 49 cases were due to affordability or forbearance (2013: four).

There are 28 accounts at 31 December 2014 (31 December 2013: four) on which interest rate concessions have been applied.

During 2014, three properties were taken into possession by the Society, one of which was sold.

At the end of 2014 the Society had 20 properties in possession representing capital balances of £2,271,415 which is 0.27% of the total Society book (2013: 0.52%). Compared to 2013 the number of cases reduced from 21 and the capital balances decreased by £1,845,485.

In Crocus there was one possession in the year (2013: nil).

The Society also engages a Receiver of Rents to manage properties on behalf of the customer, where the customer is unable to do so effectively. Where this occurs, interest concessions are applied, including interest waivers. At the end of 2014 the Group was a Receiver of Rents on 89 properties (2013: 86) representing capital balances of £13.3m (2013: £8.7m), which is 1.48% of the total Group book (2013: 1.09%). Of these properties 16 were also in possession (2013: 17), included in the values for possession cases specified above, representing capital balances of £2.0m (2013: £2.3m). This portfolio of Receiver of Rent portfolios is reviewed on an ongoing basis to ensure that potential losses to the Society are managed and mitigated. Not withstanding the active management of the portfolio, at 31 December 2014 provisions of £2.2m were maintained to protect the Society against losses (2013: £1.5m).

This provision is calculated with regard to the expected cashflow return from the portfolio, discounted at a market rate (the OIS Swap rate).

The accounts discussed above that have been identified as showing forbearance characteristics have been assessed under either the specific or forbearance provisions as detailed in Note 1h to the accounts on page 27. The forbearance provision is calculated with regard to the expected cashflow return from the portfolio, discounted at the market rate.

# Notes to the accounts (continued)

## 13. Investments in subsidiary undertakings

| | Society 2014 £000 | Society 2013 £000 |
|---|---|---|
| Shares in subsidiary undertaking | 86 | 86 |
| Loans to subsidiary undertaking | 43,257 | 45,726 |
| | 43,343 | 45,812 |
| Movement during the year of loans to subsidiary undertaking: | | |
| Cost<br>At 1 January | 45,726 | 48,169 |
| Repayments received | (2,469) | (2,443) |
| At 31 December | 43,257 | 45,726 |

The Society holds 100% of the ordinary share capital of Crocus Home Loans Limited, for the purpose of secured lending on residential property. The share capital authorised and issued is £1,000.

The Society holds 100% of Saffron Independent Financial Advisers Limited (SIFA). On 13 February 2012 the client business of this subsidiary was sold to Towergate Financial (East) Limited for a consideration of £187,500 of which £67,500 was a deferred consideration and recognised in 2013.

The following 100% owned subsidiaries were not carrying on business at the end of the financial year:

| | Share Capital |
|---|---|
| Saffron Independent Financial Advisors Limited | £85,000 |
| Saffron Walden Investment Services Limited | £2 |
| Saffron Walden Property Developments Limited | £2 |
| Saffron Walden Property Sales Limited | £2 |

All subsidiary undertakings are registered in England and Wales and operate within the United Kingdom.

## 14. Tangible fixed assets

| | Group & Society | | | |
|---|---|---|---|---|
| | Land & Buildings | | | |
| | Freehold £000 | Short leasehold £000 | Equipment, fixtures, fittings and vehicles £000 | Total £000 |
| Cost or valuation<br>At 1 January 2014 | 6,794 | 677 | 9,256 | 16,727 |
| Additions | 438 | 33 | 3,095 | 3,566 |
| Disposals | – | – | 5 | 5 |
| At 31 December 2014 | 7,232 | 710 | 12,346 | 20,288 |
| Depreciation<br>At 1 January 2014 | 796 | 59 | 3,857 | 4,712 |
| Charged in year | 151 | 67 | 1,055 | 1,273 |
| Disposals | – | – | 5 | 5 |
| At 31 December 2014 | 947 | 126 | 4,907 | 5,980 |
| Net Book Value | | | | |
| At 31 December 2014 | 6,285 | 584 | 7,439 | 14,308 |
| At 31 December 2013 | 5,998 | 618 | 5,399 | 12,015 |

Freehold Land and Buildings are held at valuation and were professionally valued by Derrick Wade Waters, Chartered Surveyors, on an existing use basis for branches and open market value for investment properties as at 31 December 2013. This valuation was £6.0m compared to a net book value of £6.4m.

The reduction in the valuation noted in the prior year has been re-classed from opening depreciation to opening valuation. This has no impact on the prior year net book value.

Should the freehold land and buildings been carried at historical cost less depreciation the carrying amount would have been £5.0m (2013: £5.1m).

The net book value of land and buildings occupied by the Society for its own activities is as follows:

| | Group and Society | |
|---|---|---|
| | 2014 £000 | 2013 £000 |
| Freehold | 3,628 | 3,462 |

# Notes to the accounts (continued)

## 15. Other assets

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Other assets | 11 | 11 | 762 | 762 |
| Deferred tax | 141 | 20 | 380 | 279 |
| | 152 | 31 | 1,142 | 1,041 |
| The elements of deferred taxation are as follows: | | | | |
| Difference between accumulated depreciation and capital allowances | (335) | (335) | (95) | (95) |
| General provision for bad and doubtful debts | 503 | 382 | 502 | 401 |
| Other timing differences | (27) | (27) | (27) | (27) |
| Deferred taxation asset | 141 | 20 | 380 | 279 |

| | Group £000 | Society £000 |
|---|---|---|
| The amounts provided are the full potential liabilities. | | |
| At 1 January 2014 | 380 | 279 |
| Deferred tax movement for the year | (239) | (259) |
| At 31 December 2014 | 141 | 20 |

The deferred tax asset is derived predominantly from short term timing differences from the tax treatment for bad debt provisions and bonus accruals offset by capital gains and accelerated allowances. The Society considers this asset to be recoverable in the foreseeable future under the normal course of business.

## 16. Shares

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Held by individuals | 952,228 | 952,228 | 915,829 | 915,829 |
| Repayable from the date of the balance sheet in the ordinary course of business as follows: | | | | |
| Accrued interest | 4,916 | 4,916 | 5,726 | 5,726 |
| On demand | 631,608 | 631,608 | 604,797 | 604,797 |
| In more than three months but not more than one year | 278,225 | 278,225 | 240,533 | 240,533 |
| In greater than one year | 37,479 | 37,479 | 64,773 | 64,773 |
| | 952,228 | 952,228 | 915,829 | 915,829 |

## 17. Amounts owed to credit institutions

| Repayable from the balance sheet date in the ordinary course of business as follows: | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Accrued interest | 551 | 551 | 526 | 526 |
| In not more than three months | 1,251 | 1,251 | – | – |
| In more than three months but not more than one year | 1,067 | 1,067 | 1,133 | 1,133 |
| In more than one year but not more than five years | 15,781 | 15,781 | 14,135 | 14,135 |
| In more than five years but not more than 10 years | – | - | 6,948 | 6,948 |
| | 18,650 | 18,650 | 22,742 | 22,742 |

# Notes to the accounts (continued)

## 18. Amounts owed to other customers

Repayable from the balance sheet date in the ordinary course of business as follows:

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Accrued interest | 414 | 414 | 305 | 305 |
| On demand | 125,700 | 125,700 | 161,187 | 161,187 |
| In more than three months but not more than one year | 13,035 | 13,035 | 28,660 | 28,660 |
| | 139,149 | 139,149 | 190,152 | 190,152 |

## 19. Other liabilities

Falling due within one year

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Income tax | 701 | 701 | 858 | 858 |
| Corporation tax | 482 | 362 | 515 | 445 |
| Other creditors | 484 | 484 | 839 | 849 |
| | 1,667 | 1,547 | 2,212 | 2,152 |

## 20. Accruals & deferred income

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Interest accrued on subordinated liabilities | 270 | 270 | 270 | 270 |
| Other accruals | 1,457 | 1,426 | 1,479 | 1,448 |
| | 1,727 | 1,696 | 1,749 | 1,718 |

## 21. Subordinated liabilities

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Fixed Rate 6.32% Subordinated Debt 2028 | 10,000 | 10,000 | 10,000 | 10,000 |

The Society entered into a subordinated liabilities issue during 2003. The issue is for £10,000,000 denominated in sterling, and the loan is repayable at maturity.

The rights of repayment of the holders of this issue are subordinated to the claims of all depositors, all creditors and members holding shares in the Society, as regards the principal of their shares and interest due to them.

## 22. General reserves

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| General reserve at start of the year | 44,026 | 42,534 | 41,801 | 40,568 |
| Actuarial (losses) net of deferred tax | (702) | (702) | (86) | (86) |
| Profit for financial year | 2,951 | 2,861 | 2,320 | 2,044 |
| Transfer of depreciation on revalued assets | 49 | 49 | 8 | 8 |
| Prior year restatement | – | – | (17) | – |
| General reserve at end of year | 46,324 | 44,743 | 44,026 | 42,534 |

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| General reserve excluding pension reserve | 49,080 | 47,499 | 46,080 | 44,588 |
| Pension reserve | (2,756) | (2,756) | (2,054) | (2,054) |
| General reserve including pension reserve | 46,324 | 44,743 | 44,026 | 42,534 |

# Notes to the accounts (continued)

## 23. Revaluation reserve

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Revaluation reserve at start of the year | 828 | 828 | 1,155 | 1,155 |
| Movement in revaluation reserve | – | – | (319) | (319) |
| Transfer of depreciation on revalued assets | (49) | (49) | (8) | (8) |
| Revaluation reserve at end of the year | 779 | 779 | 828 | 828 |

## 24. Guarantees and other financial commitments

a) Financial Services Compensation Scheme

In common with other regulated UK deposit takers the Society pays levies to the Financial Services Compensation Scheme (FSCS) to enable the FSCS to meet claims against it. During 2008 and 2009 claims were triggered against the FSCS in relation to a number of financial institutions including Bradford & Bingley plc, Kaupthing Singer & Friedlander, Heritable Bank plc, Landsbanki hf and Dunfermline Building Society.

The FSCS meets these claims by way of loans received from HM Treasury and has in turn acquired rights in the realisation of the assets of the banks. The FSCS is liable to pay interest on these loans, and may have a further liability if there are insufficient funds from the realisation of the assets of the bank to fully repay these loans.

The term of these loans was interest only for the first three years, with the FSCS recovering the interest cost, together with its own ongoing management expenses, through annual management levies on its members. The initial three year term expired in September 2011, and under the renegotiated terms the interest rate was reset from 12 month Libor +30bps to 12m Libor +100bps.

By virtue of it holding deposits protected under the FSCS scheme at 31 December 2014, the Society has an obligation to pay levies in respect of the interest cost for 2014/15. From 2013, the FSCS has also started to repay the principal of the Treasury loans and a further levy has been raised in 2014/15 for the expected capital shortfall for these loans, so that they are fully repaid by March 2016. The total levy to be raised is £961m over three years, with the second instalment of £399m collected this year.

The provision as at 31 December 2013 was £439,000 and payments of £354,000 and £433,000 were made during the year in respect of the 2014/15 capital shortfall levy and the 2013/14 interest levy. The net charge to the Income and Expenditure Account was £761,000, and the provision held at 31 December 2014 was £413,500.

b) Annual commitments under non-cancellable operating leases are as follows:

| | Group 2014 £000 | Society 2014 £000 | Group 2013 £000 | Society 2013 £000 |
|---|---|---|---|---|
| Land and buildings | | | | |
| Operating leases which expire in five years or less | 70 | 70 | 70 | 70 |
| Operating leases which expire in greater than five years but less than 10 years | 205 | 205 | 140 | 140 |
| Other | | | | |
| Operating leases which expire in five years or less | 319 | 313 | 204 | 198 |

c) At 31 December 2014, the Group had capital commitments of nil (2013: nil) which were contracted but not provided for.

# Notes to the accounts (continued)

## 25. Financial Instruments

A financial instrument is a contract which gives rise to a financial asset of one entity and a financial liability of another entity. The Group is a retailer of financial instruments in the form of mortgage and savings products and uses wholesale financial instruments to invest liquid asset balances, raise wholesale funding and manage risks arising from its operations.

The Group has a formal structure for managing risk, including establishing risk appetite, risk limits, reporting lines, mandates, policies and other control procedures. This structure is reviewed regularly by the Assets and Liability Committee (ALCO), which is charged with the responsibility for managing and controlling the Balance Sheet and the use of financial instruments for risk management purposes. Further oversight of risk management is provided by the Risk, Audit, Conduct & Compliance Committee (RACCC).

Instruments used for risk management purposes include derivative financial instruments (derivatives), which are contracts or agreements whose value is derived from one or more of underlying price, rate or index inherent in the contract or agreement, such as interest rates.

Derivatives are only used by the Society in accordance with the Building Societies Act 1986 (as amended by the Building Societies Act 1997) to reduce the risk of loss arising from changes in interest rates or other factors specified in the legislation.

Derivatives are not used in trading activity or for speculative purposes.

**Types of Derivatives**

The principal derivatives used by the Society in Balance Sheet risk management are sterling interest rate swaps which are used mainly to hedge Balance Sheet exposures arising from fixed rate mortgage lending and fixed rate borrowing. The Society also uses swaps based on the movement of inflation and equity indices to hedge Balance Sheet exposures arising from index-linked borrowing.

The table below shows the notional principal amounts, risk weighted amounts and replacement costs of derivatives. Notional principal amounts indicate the volume of business outstanding at the Balance Sheet date and do not represent amounts at risk. The risk weighted amounts, which are calculated in accordance with rules set by the regulator, reflect a measure of the extent of potential future exposure and the nature of the counterparty.

The replacement costs represent the cost of replacing contracts with positive values, calculated at market rates current at the Balance Sheet date, and reflect a measure of the Group's exposure should all counterparties default. The Society uses industry standard documentation for its derivative contracts. Most of these contracts include credit support agreements, as a result of which collateral is pledged or held, in the form of listed debt securities (usually UK gilts) or cash deposits to provide protection to both the Society and its counterparties against default. Details of this collateral are provided in the final section of this note entitled 'Fair values of financial instruments'.

Derivatives at the Balance Sheet dates are predominantly sterling interest rate swap contracts, with the rest based on the Retail Price Index, as shown in the following table.

| | 2014 Notional principal amount £000 | 2014 Risk weighted amount £000 | 2014 Replacement cost £000 | 2013 Notional principal amount £000 | 2013 Risk weighted amount £000 | 2013 Replacement cost £000 |
|---|---|---|---|---|---|---|
| Interest rate contracts | 295,003 | 375 | – | 180,675 | 405 | – |
| Under one year | 18,000 | – | – | 58,245 | 159 | – |
| Between one and five years | 229,283 | 232 | – | 73,000 | 98 | – |
| Greater than five years | 47,720 | 143 | – | 49,430 | 148 | – |
| | 295,003 | 375 | – | 180,675 | 405 | – |

**Interest Rate Risk**

The Group is exposed to interest rate risk through a number of potential mismatches. The Group manages this exposure on a continuous basis through ALCO, within limits set by the Board, using a combination of on and off-balance sheet instruments. These mismatches are primarily: interest rate basis risk, where instruments with similar re-pricing characteristics reprice differently e.g. LIBOR rates increase more quickly than mortgage rates; yield curve risks, causing assets and liabilities to reprice differently; for example where there is a mismatch between the dates on which interest receivable on assets and interest payable on liabilities are next reset to market rates. The latter interest rate sensitivity exposure for the Group, after taking into account off-balance sheet derivative hedge contracts entered into by the Society to manage this risk, was as follows:

# Notes to the accounts (continued)

## 25. Financial Instruments (continued)

**As at 31 December 2014**

| Assets | Not more than three months £000 | More than three months but not more than than six months £000 | More than six months but not more than one year £000 | More than one year but not more than five years £000 | More than five years £000 | Non-interest bearing £000 | Total £000 |
|---|---|---|---|---|---|---|---|
| Liquid assets | 132,912 | 64,893 | 4,986 | 40,865 | 9,970 | 662 | 254,288 |
| Loans and advances to customers | 603,377 | 37,813 | 2,236 | 213,407 | 46,632 | (3,538) | 899,927 |
| Tangible fixed assets | – | – | – | – | – | 14,308 | 14,308 |
| Other assets | – | – | – | – | – | 2,001 | 2,001 |
| Total assets | 736,289 | 102,706 | 7,222 | 254,272 | 56,602 | 13,433 | 1,170,524 |
| **Liabilities** | | | | | | | |
| Shares | 636,525 | 145,683 | 132,540 | 37,480 | – | – | 952,228 |
| Amounts owed to credit institutions and other customers | 135,587 | – | 1,133 | 14,135 | 6,944 | – | 157,799 |
| Other liabilities | – | – | – | – | 10,000 | 3,394 | 13,394 |
| Reserves | – | – | – | – | – | 47,103 | 47,103 |
| Total liabilities | 772,112 | 145,683 | 133,673 | 51,615 | 16,944 | 50,497 | 1,170,524 |
| Interest rate and equity swaps- asset hedge | (249,220) | (25,000) | – | (20,783) | – | – | – |
| Interest rate and equity swaps - liability hedge | – | 18,000 | – | 229,283 | 47,720 | – | – |
| Interest rate and equity swaps | (249,220) | (7,000) | – | 208,500 | 47,720 | – | – |
| Interest rate and equity swaps sensitivity gap | 213,397 | (35,977) | (126,451) | (5,843) | (8,062) | (37,064) | – |
| Cumulative interest rate and equity swaps sensitivity gap | 213,397 | 177,420 | 50,969 | 45,126 | 37,064 | – | – |

At 31 December 2014, the Group had £48m of swaps designed to protect the Society against the interest rate risk presented by its equity release portfolio. These swaps are structured within upper and lower bands and are designed to reflect the projected balances of the portfolio contained, incorporating underlying assumptions on property values, prepayments and actuarial assessments on mortality.

**As at 31 December 2013**

| | Not more than three months £000 | More than three months but not more than than six months £000 | More than six months but not more than one year £000 | More than one year but not more than five years £000 | More than five years £000 | Non-interest bearing £000 | Total £000 |
|---|---|---|---|---|---|---|---|
| Total assets | 810,527 | 97,449 | 92,192 | 115,523 | 58,090 | 13,757 | 1,187,538 |
| Total liabilities | 811,957 | 82,833 | 148,087 | 78,903 | 16,943 | 48,815 | 1,187,538 |
| Interest rate and equity swaps – asset hedge | (116,930) | (5,000) | (15,000) | (36,801) | (6,944) | – | – |
| Interest rate and equity swaps – liability hedge | 28,245 | 10,000 | 20,000 | 73,000 | 49,430 | – | – |
| Interest rate and equity swaps | (88,685) | 5,000 | 5,000 | 36,199 | 42,486 | – | – |
| Interest rate and equity swaps sensitivity gap | 87,255 | 9,616 | (60,895) | 421 | (1,339) | (35,058) | – |
| Cumulative interest rate and equity swaps sensitivity gap | 87,255 | 96,871 | 35,976 | 36,397 | 35,058 | – | – |

**Liquidity Risk**

The Group's liquidity policy is to maintain sufficient assets in liquid form at all times to ensure that the Group can meet all its liabilities as they fall due and also meet all regulatory liquidity requirements.

The Group manages this risk on a continuous basis through ALCO and by ensuring compliance with the Liquidity and Financial Risk Management Policies approved by the Board. In practice this results in the Group holding a significant amount of highly liquid assets, mainly UK gilts, Treasury bills, multilateral development bank securities and deposits with the Bank of England, which are eligible to meet its required liquidity buffer set by the regulator. The Society also holds a separate pool of such assets for use as collateral with derivative counterparties. In addition the Group maintains deposits placed on call or overnight with the Bank of England and major banks to meet its operational needs without drawing on its buffer requirements.

# Notes to the accounts (continued)

## 25. Financial Instruments (continued)

**Fair value of financial instruments**
Instruments used for hedging are accounted for on an accruals basis in line with the underlying instruments being hedged. Consequently unrealised gains and losses on such instruments are not recognised. The following table shows the gains and losses that would occur if hedging instruments were carried at market value:

| | 2014 | | 2013 | |
|---|---|---|---|---|
| | Group Book value £000 | Society Fair value £000 | Group Book value £000 | Society Fair value £000 |
| Debt securities | 197,911 | 197,911 | 270,526 | 270,526 |
| Subordinated liabilities | (10,000) | (10,000) | (10,000) | (10,000) |
| | 187,911 | 187,911 | 260,526 | 260,526 |
| Interest rate swaps | – | (30,455) | – | (13,298) |

The fair value of the interest rate derivatives attached to the equity release portfolio have increased over 2014 resulting in a negative fair value to the Society.  This is due to the flattening of the market interest rate curves through to the maturity of the instrument. This movement in fair value is offset by an increase in the fair value of the underlying mortgage assets and therefore does not represent an exposure to the Group.

The table excludes certain financial assets and liabilities which are not listed or publicly traded, or for which a liquid and active market does not exist.  It therefore excludes items such as mortgages, share accounts and bank deposits.

## 26. Country by country reporting

The Capital Requirements (Country-by-Country Reporting) Regulations 2013 introduced reporting obligations for institutions within the scope of the European Union's Capital Requirements Directive (CRD IV).

Article 89 of the CRD IV requires credit institutions and investment firms in the EU to disclose annually, specifying, by Member State and by third country in which it has an establishment, the following information on a consolidated basis for the year ended 31 December 2014:

| | |
|---|---|
| Name | Saffron Building Society |
| Type of entity | Credit Institution |
| Nature of activities | Deposit taking and mortgage lending |
| Geographical location | United Kingdom |
| Number of employees | 169 |
| Turnover | £37,113,000 |
| Pre-tax profit | £3,781,000 |
| Corporation tax paid | £631,000 |
| Public subsidies received | £nil |

Turnover is derived from the Income and Expenditure Account as Interest receivable and similar income, plus Pension finance income, plus net Fees and commissions income, plus Other operating income.

# Annual business statement

for the year ended 31 December 2014

## 1 Statutory percentages

| | Ratio at 31 Dec 2014 % | Statutory limit % |
|---|---|---|
| Lending limit | 0.6 | 25 |
| Funding limit | 14.2 | 50 |

The above percentages have been calculated in accordance with the provisions of the Building Societies Act 1986.

The lending limit measures the proportion of business assets other than in the form of loans fully secured on residential property. Business assets are the total assets of the Group plus provisions for bad and doubtful debts less liquid assets and tangible fixed assets.

The funding limit measures the proportion of shares, deposits and debt securities not in the form of shares held by individuals.

The statutory limits are prescribed in Building Society legislation and ensure that the principle purpose of a Building Society is that of making loans which are secured on residential property and are funded substantially by its members.

## 2 Other percentages

| As a percentage of shares and borrowings | Ratio at 31 Dec 2014 % | Ratio at 31 Dec 2013 % |
|---|---|---|
| Gross capital | 5.1 | 4.9 |
| Free capital | 4.1 | 4.1 |
| Liquid assets | 22.9 | 29.1 |
| As a percentage of mean total assets: | | |
| Profit after taxation | 0.25 | 0.19 |
| Management expenses | 1.19 | 1.00 |

The above percentages have been prepared from the Group accounts:

Shares and borrowings' represent the total of shares, amounts owed to credit institutions and amounts owed to other customers, in each case including accrued interest.

'Gross capital' represents the aggregate of reserves, revaluation reserves and subordinated liabilities.

'Free capital' represents the aggregate of gross capital and general provisions for bad and doubtful debts less tangible fixed assets.

'Liquid assets' represent the total of cash in hand and balances with the Bank of England and loans and advances to credit institutions.

'Mean total assets' represent the average of total assets at the beginning and the end of the financial year

'Management expenses' represent the aggregate of administrative expenses and depreciation shown in the Group Income and Expenditure Account

# Annual business statement (continued)

for the year ended 31 December 2014

### 3. Information relating to the Directors and other Officers as at 31 December 2014

| NAME OF DIRECTOR | DATE OF BIRTH | DATE OF APPOINTMENT | OCCUPATION | OTHER DIRECTORSHIPS |
|---|---|---|---|---|
| T G Barr | 22.11.1962 | 10.04.2014 | Director | Crocus Home Loans Ltd<br>IT Range Ltd |
| G R Dunn | 10.07.1949 | 26.05.2011 | Director | Crocus Home Loans Ltd<br>Saffron Independent Financial Advisers Ltd<br>Citadele Banka SC, Latvia |
| C H Field | 24.11.1973 | 1.05.2014 | Chief Financial Officer | Crocus Home Loans Ltd |
| N J Holden | 7.12.1959 | 27.03.2014 | Director | Crocus Home Loans Ltd<br>Bank of London & The Middle East plc<br>Integrated Financial Arrangements plc<br>Stanbic International Insurance Ltd<br>Calmindon Ltd |
| S A Howe | 28.05.1965 | 1.05.2014 | Chief Customer Officer | Crocus Home Loans Ltd |
| J E Smith | 05.04.1947 | 28.04.2005 | Director | Crocus Home Loans Ltd<br>Saffron Independent Financial Advisers Ltd<br>The Virtual Company Ltd<br>Council for Conveyancers |
| N J Treble | 24.08.1959 | 27.03.2014 | Director | Crocus Home Loans Ltd<br>Batesons Consulting Ltd |
| C R L Wilson | 21.11.1949 | 23.07.2009 | Director | Crocus Home Loans Ltd |

Documents may be served on the above-named Directors at the following address:
Deloitte LLP, Four Brindleyplace, Birmingham, B1 2HZ

| OTHER OFFICERS | DATE OF BIRTH | DATE OF APPOINTMENT | OCCUPATION | OTHER DIRECTORSHIPS |
|---|---|---|---|---|
| R J Barrett | | | Chief People Officer<br>& Society Secretary | Saffron Independent Financial Advisers Ltd<br>The Flitch Green Academy |
| J M Claydon | | | Chief Operating Officer | Impirica Ltd |
| F M McNeill | | | Chief Risk Officer | McNeill Finance & Risk Solutions Ltd |

### 4. Directors service contracts

As at 31 December 2014, C H Field and S A Howe had service contracts with the Society which could be terminated by either party giving six months notice.

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1A Market Street,
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Saffron Building Society