STAFFORD RAILWAY
BUILDING SOCIETY

Pillar 3 Disclosure Document

For The Year Ended 31 October 2017

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STAFFORD RAILWAY
BUILDING SOCIETY

1. Introduction

The Stafford Railway Building Society ("the Society") has an obligation to ensure that its members are protected by setting aside an adequate amount of capital for the prevailing economic conditions. Internal systems and controls have been designed to predict potential losses which may arise from mortgage lending and operational risks under stressed conditions.

The purpose of this document is to provide members with background information on the Society's approach to risk management and the maintenance of its capital strength. As such, it includes details of:

- The Society's approach to risk management, its policies and objectives;
- The governance structure of the Board and Board Committees;
- Own funds information (or capital resources);
- Regulatory capital requirements; and
- Compliance with the European Union (EU) Capital Requirements Regulation

2. Basel III framework

The legislative framework under which the Society operates are European standards for capital and liquidity requirements for banks, building societies and related institution set out in the Capital Requirements Directive IV (CRD IV, 2013/36/EU) and the Capital Requirements Regulation (CRR, 575/2013). This legislation came into force on 1 January 2014 and is the European implementation of Basel III, which sets out global standards for capital and liquidity adequacy.

Prudential supervision with regards to capital and liquidity adequacy is overseen in the UK by the Prudential Regulation Authority (PRA), and CRD IV is implemented in the PRA Rulebook. CRR on the other hand is directly applicable, without implementation in national legislation, CRD IV and CRR are supported by additional guidance and standards defined both on a European and on a national level.

CRR sets out not only capital requirements, but also specifies what the Society must disclose in regard to its risk management policies, procedures, and performance, including the main risks faced by the Society and the governance of those risks. These disclosure requirements are usually referred to as "Pillar 3", being the third pillar of the three-pillar approach which is normally considered for prudential banking regulation.

Pillar 1 – this is a risk-based calculation with an emphasis on credit risk and operational risk and sets out the minimum capital requirements the Society needs to adhere to. The Society uses the standardised approach to calculate credit risk, applying standardised risk weightings to mortgage lending, treasury assets and all other assets. Capital required to cover operational risk is assessed under the Basic Indicator Approach and calculated by reference to the net income of the Society averaged over the previous three years.

Pillar 2 – this is the framework for the assessment of risk that is not fully covered by Pillar 1 or risks that are not within the scope of Pillar 1. The self-review of Pillar 2 is documented in the Society's Internal Capital Adequacy Assessment (ICAAP) which is approved annually by the Board and is subject to review by the PRA, providing a view on Society specific risks and calculating a forward looking buffer for capital planning that takes account of capital requirements under economic stress. Additional buffers that consider capital needs over the economic cycle are the Capital Conservation Buffer from the European Banking Authority (EBA) and the UK Counter-Cyclical Buffer set by the Financial Policy Committee (FPC).

Pillar 3 – this builds on work undertaken as part of the ICAAP and discloses key elements to the industry and to our members on the Society's capital resources, risk exposures and risk management processes. This document contains the requirements for Pillar 3 (disclosure), and the information provided here is in accordance with the rules and guidance contained in CRD IV.

In addition to the assessment of capital requirements under Pillar 1 and 2 above, the Society's overall capital requirement is reviewed periodically by the PRA. The PRA set the minimum amount of capital they consider that the Society should hold.

3. Basis of preparation

The Pillar 3 disclosures have been prepared in order to explain the basis on which the Society has prepared and disclosed certain capital requirements and information about the management of certain risks and for no other purpose. The disclosures do not constitute any form of financial statement and must not be relied upon in making any judgement on the Society. There is no requirement for the disclosures to be externally audited.

The information presented is based on the Society's Annual Report and Accounts as at 31 October 2017, but may differ where regulatory requirements differ from the requirements underlying the Annual Report and Accounts. Consistent with regulatory reporting for capital adequacy purposes, the Society information from the Annual Report and Accounts has been used.

CRD IV introduced a country-by-country reporting requirement aimed at providing transparency of a financial institution's income and the location of its operations. This is reported at note 25, on page 65, in the Annual Report and Accounts. The Society's Annual Report and Accounts are published on the Society's website (www.srbs.co.uk).

The Board of Directors can confirm that the Society's current capital position, in its opinion, is sufficient to meet the minimum capital resources requirement and that sufficient capital will continue to meet minimum requirements for its planned future strategy. In addition, risk management arrangements adequately assess and control the principal risks facing the Society and are proportionate in light of the characteristics, size, scale and complexity of the Society.

In the event that a user of this document requires further explanation on the disclosures given, application should be made in writing to the Chief Executive or the Finance Director at Stafford Railway Building Society, 4 Market Square, Stafford ST16 2JH.

4. Verification, location and frequency of risk disclosure

This document is reviewed annually by the Society's Risk Committee and approved by the Board and published on the Society's website (www.srbs.co.uk) within six months of the financial year-end, that is, by 30 April 2018.

The Society's Annual Report and Accounts are published on the Society's website (www.srbs.co.uk) and can be accessed there to act as a reference point.

5. Scope of application

The disclosure requirements in this document apply to the Society. The Society has no subsidiaries.

6. Risk Management Policies and Objectives

6.1. Information on governance arrangements

A summary of the relevant experience of the Executive and Non-Executive Directors is given on page 17 of the Annual Report and Accounts.

A summary of the directorships held by each Executive and Non-Executive Director is held within the Annual Business Statement on page 68 of the Annual Report and Accounts.

The Society's Annual Report and Accounts are published on the Society's website (www.srbs.co.uk).

As reported in the Annual Report and Accounts for 31 October 2016, the Society commenced the process of succession planning for Susan Whiting, Chief Executive and Jeremy Hodgkiss, Finance Director and Deputy Chief Executive last year, and was successful in recruiting Michael Smith to the role of Chief Executive on 9 October 2017. Michael Smith is employed directly by the Society. The contract with Deans (Staffordshire) Limited provides the services of Finance Director, Deputy Chief Executive and Secretary while the recruitment process for these roles continues.

The Society's Non-Executive Directors are recruited from a range of appropriate backgrounds, ensuring they have the necessary breadth of skills, knowledge and experience to monitor the performance of the Society and to challenge the Executive in a constructive manner.

The Board considers that all its Non-Executive Directors are independent and free of any relationship which could materially interfere with the exercise of their judgement. Under the terms of the UK Corporate Governance Code (2016), factors to be taken into account when assessing independence include length of service and whether the Director has recently been an employee of the Society. Colin Lloyd is the Senior Independent Director to whom members may address any concerns or issues they may wish to raise. However, all Directors are happy to make themselves available to members for such purposes.

All Non-Executive vacancies are advertised to members and the Nominations Committee makes appointments having considered the balance of skills and experience required. All Directors must meet the test of fitness and propriety as laid down by the PRA as Approved Persons to fulfil their Controlled Functions as Directors. The Board is mindful of the Davies Report on diversity and has disclosed information on gender mix in the Directors' Report on page 16 of the Annual Report and Accounts.

During the recruitment process applicants are advised on the time requirement for proper discharge of their duties. Their ability to commit sufficient time is assessed during their evaluation on appointment and as part of the formal appraisal process. Details of Board and Committee attendance throughout the year are shown on page 24 of the Annual Report and Accounts.

New Directors receive full and formal induction training and all Directors are provided with on-going training and professional development to provide continual updating of their skills. Training is provided in a range of appropriate forms including in-house training, industry events, seminars and conferences.

6.2. Risk management structure

The Society has adopted a "three lines of defence" approach to the operational management of the firm. This approach ensures that staff are aware of their responsibilities and that an effective segregation of duties is in place across the Society. This is illustrated below:

1. First line of defence – Operational Management

The Society's managers are in the best position to assess and manage the risk exposures within their teams. The management identify, assess, and manage risk through normal business operation. Any breaches are reported to Executive and through the governance structure as appropriate.

2. Second line of defence – Risk and Compliance function

The second line of defence is responsible for challenging of risks, policies and controls in place. This function is operationally independent from the business managers and can therefore uphold the principles and policies of the Society. They provide oversight of the first line functions and independently report to Risk and/or Audit Committees any policy breaches or control issues.

3. Third line of defence – Internal Audit and External Audit

Internal Audit is entirely independent of the operational functions of the Society and reports directly to the Audit Committee. The function is outsourced to Deloitte LLP to ensure further independence. Their role is to independently confirm that all activities are within policy, legal or regulatory requirements.

External audit is independent and provided by KPMG LLP with a reporting line direct to the Audit Committee.

Line of defence	Responsibility	Oversight
1st	Management	CE and FD
2nd	Risk and Compliance Manager, MLRO	Risk Committee, Remuneration and Nomination Committee
3rd	Internal Audit (outsourced) External Audit	Audit Committee, Board

Where:

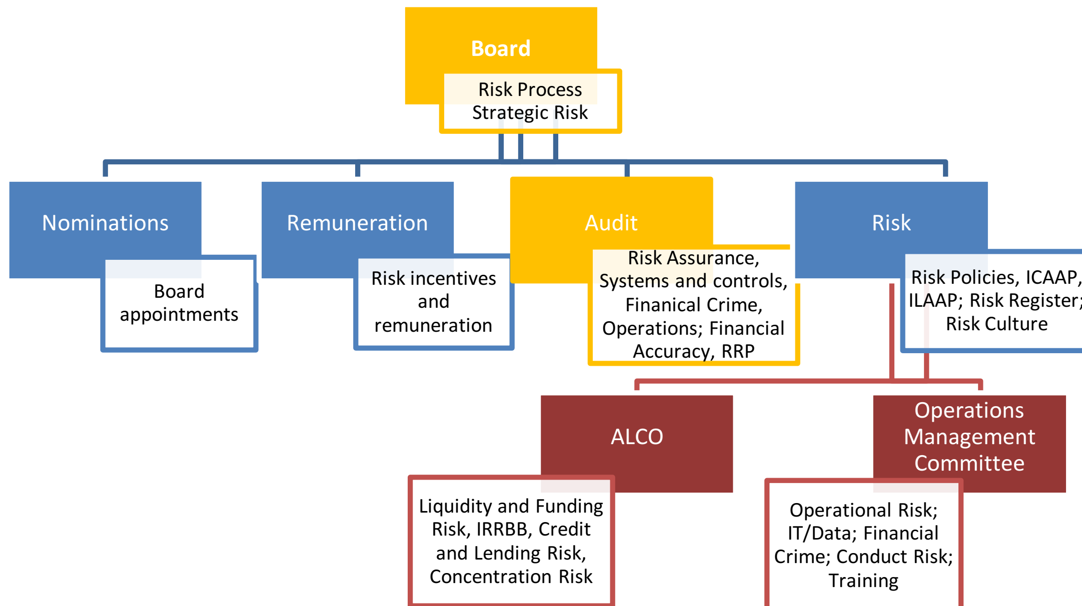
- CE: Chief Executive
- FD: Finance Director
- MLRO: Money Laundering Reporting Officer

6.3. Risk management organisational and governance structure

The Society's Board has ultimate responsibility for developing an appropriate risk and control framework. The Board comprises three Executive Directors and six Non-Executive Directors and meets eleven times a year. The Board of Directors comprises professional and business people from a variety of backgrounds. It is recognised that an appropriate mix of skills and diversity is required on the Board, but that this must be balanced with increasing pressure to have sector and risk management experience to satisfy Regulatory requirements. It is also recognised that to obtain this mix, the Society has to look beyond its local area, although maintaining links with the local community is very important.

The Board is responsible for setting the overall risk strategy and approving the design and implementation of risk management approaches, including the risk management framework policy, the risk appetite statements and the metrics that underpin them. It delegates authority for cascading the setting and approval of the more granular limits and tolerances to the Chief Executive.

The Board and Committee structure is set out below:



Where:
1st line - ALCO and Operations Management Committee (OMC)
2nd line – Nominations, Remuneration and Risk Committees
3rd line – Board and Audit Committee

IRRBB: Interest rate risk in the banking book
ICAAP: Internal Capital Adequacy Assessment Process
ILAAP: Internal Liquidity Adequacy Assessment Process
RRP: Recovery and Resolution Plan

In principle, each of the Board committees fulfil a similar role, in that, operating under a Board delegated mandate, they provide a forum for the direction and challenge of Management whilst monitoring business performance and risk exposures. Each of the Board committees comprises Non-Executive Directors with other attendees being drawn from the Executive and Senior Management. The current terms of reference for the ALCO, Audit and Risk Committees are published on the Society's website (https://srbs.co.uk/ about-us/the-board). The key committees are:

6.3.1. Audit Committee

This Committee consists entirely of Non-Executive Directors, is chaired by Colin Lloyd and meets at least four times a year. Other members of the Committee are Karen McCormick and Nicholas Sandy. Representatives from the Society Executive and Risk and Compliance functions together with the Society's internal and external auditor also attend Committee meetings by invitation. The Committee has overarching responsibility for the Society's systems and controls and considers all matters of an audit nature applying to the Society, including internal controls, compliance, scope and content of internal and external audit work, financial reporting and other relevant prudential requirements. It validates the financial statements of the Society.

A dotted line for reporting exists directly between the Chairman of the Audit Committee and the Risk and Compliance Manager.

6.3.2. Risk Committee

This Committee is chaired by Gary Crowe, following the retirement of David Gage. It meets at least quarterly during the year and advises the Board on the overall risk appetite, tolerance and strategy

and reviews the risk management framework and policies. The other members of the Committee are James Dean (Chairman) and David Grant. Representatives from the Society Executive and Risk and Compliance functions also attend Committee meetings by invitation.

In particular, the Committee monitors and reviews the consolidated risk picture across the Society. It is responsible for the on-going development and maintenance of the ILAAP and the ICAAP as well as the risk management framework. It also provides support and challenge for the development of the strategic plan and adequate stress testing strategy. The Committee receives standing reports on the Risk Register along with detailed risk management information that enables it to track performance against the risk appetite.

A dotted line for reporting exists directly between the Chairman of the Risk Committee and the Risk and Compliance Manager.

6.3.3. Assets and Liabilities Committee (ALCO)

The Committee comprises both Executive Directors and members of the management team. It meets on a monthly basis and monitors and controls balance sheet risk, funding and liquidity in line with the Society's policies. The Committee is chaired by Susan Whiting (Finance Director) and reports to the Risk Committee. Other members of staff and Non-Executive Directors attend as required. The Committee is responsible for ensuring that the Society's treasury risks (liquidity, treasury counterparty risk, interest rate risk in the banking book) are managed and mitigated in line with the Board's risk appetite and related policies. The Committee also ensures that all (non-treasury) lending undertaken by the Society is in line with the Board's risk appetite. The Committee reviews on-going management information and is responsible for recommending changes to credit policies for Board approval.

The Committee reports and escalates breaches to the Risk Committee.

6.3.4. Operations Management Committee (OMC)

This Committee comprises the Chief Executive and members of the management team, and is chaired by Michael Smith (Chief Executive). The Committee meets monthly and is responsible for organising and co-ordinating the day-to-day management of the Society, including financial crime, operational risk, and conduct risk and information technology, in line with the Board's risk appetite, Corporate Plan and overall strategic direction. Other members of staff and Directors attend as required.

The Committee reports and escalates breaches to the Risk Committee.

6.3.5. Remuneration Committee

This Committee comprises all the Non-Executive Directors under the chairmanship of Karen McCormick and is responsible for compliance with relevant elements of the Financial Conduct Authority (FCA) Remuneration Code. The basis of remuneration is consistent with sound and effective risk management and does not encourage excessive risk-taking. The Committee meets at least once per year to consider the remuneration and other terms of service of the Executive Directors and the Risk and Compliance Manager.

The overarching purpose of the Committee is to set remuneration policies to ensure that they are in line with the Society's business strategy, risk appetite and long-term objectives. This includes designing and implementing the reward structure of the Society and ensures that effective risk management is a key component of remuneration and incentive structures.

6.3.6. Nominations Committee

The Nominations Committee is chaired by the Chairman of the Board, James Dean. It also comprises Nicholas Sandy (Vice Chairman) and Colin Lloyd (Senior Independent Director). It identifies and recommends to the Board candidates for nomination as Directors and considers Board

succession planning. It meets when there is an appropriate vacancy to fill but in any case at least once a year to review the skills mix of the Board and succession planning.

6.4. Risk strategy

The Society recognises that the delivery of the Board's strategy gives rise to a number of potential risks that are inherent in the business activities of the Society. Whilst these risks can never be eliminated, through careful management they can be mitigated. The Board has agreed a risk appetite that seeks to limit the amount of risk accepted by the Society in pursuit of its Corporate Plan, helping the Society achieve sustainable growth and serving the best interests of its members and customers.

The risk management framework assists in defining the boundaries within which management is expected to operate when pursuing the Society's business strategy.

6.5. Risk management framework

The principal purpose of the Society is to make loans for the purchase and improvement of residential property and to encourage savings by offering our members competitive savings rates and a truly personal service.

The Society views risk management as an integral part of good internal control and corporate governance and puts the safety and security of members' deposits above everything else. Appropriate management and minimisation of the risks arising from business activities achieve this.

The risk management framework policy is reviewed annually by the Risk Committee and then approved by the Board.

It is acknowledged that risk is inherent in the business activities of the Society and can never be fully eliminated. The framework assists in defining the boundaries within which management is expected to operate when pursuing the Board approved business strategy and to give the best outcomes for customers.

A sound risk culture supporting appropriate risk awareness, behaviours and judgements about risk-taking within a strong governance framework is recognised as a key element in ensuring the successful operation of the Society framework.

To ensure that the framework operates effectively and efficiently the Society has adopted the three lines of defence model and defined clear governance structures for the operation of the framework.

Risks are assessed using both a qualitative and quantitative approach. The qualitative risk assessments are undertaken through risk reviews whilst a number of risk appetite measures have been defined to represent the quantitative assessments.

The risk management framework identified principal risks as being most material to the Society. The Society appoints a Risk Framework Owner (RFO) for each risk, the risk framework must be defined and documented; this comprises a principal risk policy, second level policy (if applicable), procedures and standards and risk appetite tolerance metrics.

More granular policies are reviewed and recommended by the relevant oversight Committee before Board approval. These policies set out the key risks, how they are managed and incorporate further limits and triggers which are monitored in more detail by management committee(s) and reported to Board Committee as appropriate.

In addition, the third line of defence review the operation of controls during their assessments to provide assurance to the Audit Committee that controls are operating as expected or where weaknesses are identified to assist the strengthening of the risk management framework.

Risk management information includes a Risk Dashboard which reflects the Board's Risk Appetite Statement and is monitored by ALCO and OMC, the Risk Committee and the Board at all of their meetings. In addition, the higher risk items from the Risks and Controls Register are reviewed at

each Board meeting. The risks in the Risks and Controls Register are an intrinsic part of the ICAAP process, which requires an assessment of key risks and a quantification of how much capital must be held to mitigate those risks.

Any changes to risks, or new and emerging risks, are identified and communicated to the Executive at management meetings. The Risk and Compliance Manager is responsible for updating risk documentation for presentation to the Risk Committee and Board. Decisions by the Board in respect of policies, risk appetite, management information required, limits and triggers on key risk indicators or risks and controls are communicated to the management team who amend the risk documentation, policies and operational procedures and train appropriate staff.

Stress tests are an integral part of the annual business planning process and annual review of risk appetite. Tests are designed to ensure that the Society's financial position and risk profile provide sufficient resilience to withstand the impact of severe economic stress on the market (systemic stress) or Society-specific stress events. Stress testing also informs early-warning triggers, management actions and contingency and recovery plans to mitigate or avoid potential stresses and vulnerabilities and as such is integral to the risk management framework. The stress-testing framework also includes reverse stress testing techniques that aim to identify circumstances under which the Society's business model could be rendered unviable, leading to a significant change in business strategy. Examples include extreme macroeconomic downturn scenarios (for example, an unemployment or credit default) and targeted attacks on the Society (for example cyber threats). Stress testing is used to identify, assess and quantify the potential effectiveness of management actions that could be taken to mitigate the impact of a stress.

7. Principal policies by category of risk

7.1. Credit Risk

Definition:
Credit risk is the risk that a borrower or counterparty to a contract will be unable or unwilling to meet their obligations as they fall due. For the Society, this normally means the risk that a borrower will not repay their mortgage loan, or that a financial institution will not repay funds invested by the Society in that institution.

Risk appetite statement:
A prudent lending approach to mortgage customers and treasury counterparties to minimise default rates and impact on profit or capital whilst generating an appropriate level of return reflecting the risk.

Key mitigating actions and processes:
The ALCO is responsible for monitoring the arrears profile through arrears, forbearance and possession reports and treasury counterparty risk through reviews against policy and reviews provided by the Society's treasury brokers. The Board approves changes to counterparties, treasury or lending policy.

Mortgage credit risk is outlined in the Society's Board approved lending risk policy and managed through the Society's underwriting process that seeks to ensure that borrowers only assume a debt that they can afford to repay. All mortgage applications are rigorously assessed with reference to the Society's lending policy. No matter how prudent lending is, however, some members can get into financial difficulties. In such circumstances, the Society is highly proactive in providing support that can include working with them to clear arrears, making arrangements, or forbearance.

The Society's lending policy details the limits set on the Society's lending operations. The Society's lending book is predominantly secured on residential property. The criteria applied to individual mortgages, and the limits set on different types of mortgages are designed to reduce to a minimum the probability of any loss from lending.

Counterparty and country limits mean that there is little concentration of treasury assets. The institutions that the Society invests in are highly rated (at least A-) and the asset types and limits have been agreed with the Regulator as compatible with their guidance to the Society under the

Supervisory Statement (SS) 20/15 Supervising building societies' treasury and lending activities. The limits are monitored through the weekly liquidity report.

7.2. Strategic Risk

Definition:
Strategic risk is the risk that the Society fails to execute its strategic plan or fails to effectively execute elements of its strategic plan due to poor planning or changes in the strategic environment.

Risk appetite statement:
The Society will obtain adequate capital generation to make the business sustainable within its chosen market. The Society will maintain sufficient capital, quality and quantity, to cover existing and projected risk in extreme but plausible scenarios and maintain market confidence.

Key mitigating actions and processes:
Strategic risk is managed through regular review and development of key performance indicators, management oversight and an embedded corporate governance framework. This includes recovery and resolution plans and specific stress testing (see section 6.1) is undertaken on an annual basis to assess the impact on the Society's Corporate Plan and desired outcomes.

7.3. Liquidity Risk

Definition:
Liquidity risk is the risk that the Society is not able to meet its financial obligations as they fall due or can only do so at excessive cost. The Society's Board approved liquidity and funding policy is to maintain sufficient liquid resources to cover cash flow requirements and fluctuations in funding, to maintain full public confidence in the solvency of the Society and to meet its financial obligations.

Risk appetite statement:
The Society will maintain sufficient liquid assets to retain members' and depositors' confidence and maintain a buffer over regulatory and internal assessments of liquidity requirement.

Key mitigating actions and processes:
This is achieved by maintaining a prudent level of liquid assets and through management control of the growth of the business. The Society holds a buffer of high quality liquid assets such as UK Treasury Bills, government securities and deposits in a Bank of England reserve account as part of regulatory requirements. The Society's approach to liquidity risk is documented in the Society's ILAAP.

The Society had no wholesale funded liabilities at any point during the year. The Society has deleted the option of wholesale funding, via broker, as a viable option under its recovery plan and advised the PRA of this earlier in 2017.

Liquidity is monitored daily by the Executive and senior management, reviewed at ALCO meetings, and included in the Management Information for Board meetings.

7.4. Interest Rate Risk

Definition:
The Society's interest rate risk arises from the impact changes in interest rates have on the Society's cash flows. The Society does not have any fixed rate savings or mortgage products, only variable, and therefore the interest rate risk for the Society is significantly less than for other similar institutions. The Society's main exposure to interest rates arises from its investment in Government Gilts and Certificates of Deposit with other financial institutions.

Risk appetite statement:
The Society aims to minimise potential losses on interest rate positions from adverse movements in market rates to ensure they remain within forecast market expectations.

Key mitigating actions and processes:

The Society uses specialist external treasury advisers for investing surplus funds and has a good spread of maturity of its invested monies to manage this risk effectively.

For further details, see Section 17 Interest Rate Risk in the Banking Book on page 22.

7.4.1. Basis and Market Risk

Definition:
Basis and market risk is the risk of an impact on economic value due to pricing assets and liabilities according to different interest rate bases. The Society's basis risk arises from assets and liabilities being linked to different interest rate types including:

- Fixed rates – treasury bills and term deposits (with other banks and other building societies);
- LIBOR – reinvestment risk on term deposits;
- Managed rates – the majority of shares and deposits; and
- Zero rates – the Society's capital and fixed assets

Risk appetite statement:
The Society aims to minimise potential losses on basis risk positions from adverse movements in market rates to ensure they remain within forecast market expectations.

Key mitigating actions and processes:
A basis risk analysis is prepared monthly and reviewed by ALCO. New products and treasury activities are assessed by ALCO taking into account their impact on the Society's basis risk exposure.

Note that the Society does not undertake any hedging in line with its approach to treasury management.

7.5. Operational Risk

Definition:
Operational risk is the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. This includes financial crime, fraud, data protection and technology and cyber risk amongst others.

Risk appetite statement:
The Society will maintain sufficient operations and robust controls to ensure that the Society's operational resilience is maintained. The Society will use technology to improve services and to safeguard members' information and the Society's systems from internal and external threats.

Key mitigating actions and processes:
The Society manages this risk by having a strong and effective internal control environment in which risks are monitored and controlled on a timely basis. Controls have been established and are maintained for all business areas. These controls appropriately address identified risks and ensure good conduct of the business in accordance with the Society's policies and risk appetite and compliance with relevant laws, regulations and rules.

The Society is extremely mindful of the threats which cyber-crime presents to all businesses. Whilst taking all reasonable precautions to mitigate this, it also has a comprehensive insurance policy to protect members in the event of such criminal activity.

The Society considers that its simple product range, robust systems, policies and internal control framework are the major factors in the achievement of strong control of operational risk. The main operations and controls are summarised in the Risks and Controls Register which is reviewed by the Risk Committee, both Internal and External Auditors and the Board.

7.6. Regulatory Risk

Definition:
Regulatory risk is the risk that the volume and complexity of regulatory issues may impact the Society's ability to compete and grow, or result in fines, public censure or restitution costs because of a failure to understand, interpret and comply with UK and EU regulatory requirements.

Risk appetite statement:
The Society will maintain good regulatory relations and systems and controls to ensure that all regulatory expectations are met and reported on within agreed and mandated timeframes.

Key mitigating actions and processes:
The Society has an internal compliance function to monitor compliance with existing legislation, the implementation of controls and the impact of new requirements. This is overseen by the Audit Committee.

7.7. Conduct Risk

Definition:
Conduct risk is the risk that the Society does not treat its members (customers) fairly and of inappropriate or unsatisfactory consumer outcomes. The Board acknowledges the requirement to fully embrace the Financial Conduct Authority (FCA)'s Principle 6, namely to ensure that the Society pays due regard to the interests of its customers and to treat them fairly at all times.

Risk appetite statement:
The Society's conduct will be maintained at a high standard and will aim to achieve desired outcomes to its members.

Key mitigating actions and processes:
These principles are firmly embedded within the Society's culture. This ethos has manifested itself into working practices throughout the Society.

The Audit Committee and the Board monitor the risk. In addition, the Risk Committee reviews and challenges the conduct risk management information. The Board reviews the conduct risk policy annually and receives conduct risk monitoring information monthly.

7.8. People Risk

Definition:
People risk refers to the costs that may arise because of matters such as discrimination, employee compensation, health and safety, training and competency and key man risk. This risk area also addresses remuneration and recruitment as well as the nomination of directors.

Key mitigating actions and processes:
The Society's employees are vital to delivering and managing the risk framework. The Society manages this risk through the operational management structure, specific policies and standards as well as management information reported to the Operations Management Committee (OMC) and Risk Committee.

For specific remuneration disclosure see section 18 below.

8. Capital Adequacy

On an annual basis, the Society updates its five-year Corporate Plan, incorporating forecast strategic business growth and capital positions and requirements. This planning cycle is driven by current market and economic conditions and is underpinned by the Society's risk appetite.

The Society's policy is to maintain a strong capital base to maintain member, creditor and market confidence and to sustain future development of the business. The formal ICAAP assists the Society with its management of capital. The Board monitors the Society's capital position monthly to assess whether adequate capital is held to mitigate the risks it faces in the course of its business activities. The Society's actual and expected capital position is reviewed against the stated risk appetite that aims to maintain capital at a level that equates to or exceeds its minimum capital requirement.

The Board manages the Society's capital and risk exposures to maintain capital in line with regulatory requirements that include monitoring of:

- Lending decisions – The Society maintains a comprehensive set of sectoral limits in its lending policy in order to manage credit risk appetite. Individual property valuations are monitored against House Price Index (HPI) data and updated quarterly.
- Concentration risk – The design of lending products takes into account the overall mix of the loan portfolio to manage exposure to risks arising from the property market and other markets the Society is active in. This is done by considering the Society's single name exposure and setting appropriate limits on individual lending, sectoral exposure to different industries for the Society's commercial lending and the Society's deliberate geographical concentration of lending solely on properties in England and Wales.
- Counterparty risk – Wholesale lending is only carried out with approved counterparties in line with the Society's lending criteria and is subject to a range of limits that reflect the risk appetite of the Society.
- Pricing – the Society's mortgages pricing model includes a capital assessment and is used to provide guidance as to the level of interest required to ensure an appropriate return is achieved.

Stress tests are used as part of the process of managing capital requirements and the ICAAP.

9. Capital Resources (at 31 October 2017)

During the year ended 31 October 2017, the Society complied with all of the externally imposed capital requirements as laid down by the PRA. During 2017, the Society has continued to comply with the EU Capital Requirements Regulation and Directive (Basel III) as amended by the PRA. Under the current PRA definitions, the Society's capital is structured as follows:

Capital resources	As at 31 October 2017 £000	As at 31 October 2016 £000
Common Tier 1 capital		
General reserves	20,232	19,501
Other reserves	(43)	24
Total Common Tier 1 capital	20,189	19,525
Tier 2 capital		
Collective provision	179	273
Total Regulatory Capital Resources	20,368	19,798

Reserves are only eligible to be treated as capital once the Annual Accounts have been independently assessed by the Society's auditors; therefore the Society's capital is only updated annually following the financial year-end.

Tier 1 capital:
These are the general reserves of the Society and represent an accumulation of after-tax profits of the Society and the available-for-sale reserve. Tier 1 capital as a percentage of risk-weighted assets is 24.57%.

Tier 2 capital:
This is the collective provision of the Society.

Capital buffers:
Basel III requires the use of common equity capital buffers to ensure that a firm has sufficient loss absorbing capital that provides a financial cushion against difficulties that might arise in times of stress.

These include a Capital Conservation Buffer of 2.5% of risk weighted assets and a Counter-Cyclical Buffer of up to 2.5% of risk weighted assets which can be applied by the regulator when macroeconomic conditions dictate. In addition, globally systemically important banks are expected to hold a buffer of up to 2.5%, but this is not applicable to the Society.

As shown above, the available Tier 1 capital at 31 October 2017 was £20.189million, and the total risk weighted assets for the Society were £82.160million, leading to a capital requirement at 8.0% of £6.573million.

As the Society currently has £13.795million of capital in excess of minimum capital requirements this is regarded as being more than sufficient to meet any future capital buffer requirements. The capital buffers are to be implemented gradually through to 2019. The Society's five year plan forecasts that the Society's capital position will strengthen over this time period and that Basel III capital requirements will continue to be met with a robust margin.

10. Risk Weighted Assets and Capital Requirements under Pillar 1

In order to produce a detailed capital plan, the ICAAP contains calculations of the capital resources requirement (effectively, the minimum capital requirement) each year using the standardised approach for credit risk and the Basic Indicator Approach (see section 11) for operational risk.

Under the standardised approach for credit risk, the Society applies a risk weighted asset value to each of its exposure classes and provides 8% of that risk weighted asset value as the minimum total capital requirement for credit risk, as follows:

	Balance sheet exposure £000	Risk weighted exposure £000	2017 Capital required £000	2016 Capital Required £000
Liquidity:				
Cash	94	-	-	-
Central Banks and Government	58,318	-	-	-
Institutions	33,458	14,186	1,135	1,588
Total liquidity	**91,870**	**14,186**	**1,135**	**1,588**
Loans and advances to customers:				
FSRP < 80% LTV	166,051	57,990	4,639	4,672
FSRP > 80% LTV	758	333	27	11
FSRP in arrears	200	262	21	40
Other mortgage assets	3,589	1,575	126	346
Total Loans and advances to customers	**170,598**	**60,160**	**4,813**	**5,069**
Other exposures:				

Fixed and other assets	670	670	53	49
Total credit risk exposures	**263,138**	**75,016**	**6,001**	**6,706**
Off balance sheet exposures	8,638	0	0	0
Market risk			0	0
Operational Risk		7,144	572	567
Total Pillar 1 capital requirement		**82,160**	**6,573**	**7,273**
Total Capital Available			20,368	19,798
Excess of Capital over Minimum Capital Requirement under Pillar 1			**13,795**	**12,525**

Where:
FSRP – fully secured on residential property

The primary differences in the 2017 Total Pillar 1 capital requirement compared to 2016 relate to liquidity and other mortgage assets. As regards liquidity, this is due to the elimination of exposures to overseas counterparties to accord with the Administered Approach to treasury management and usage of the Bank of England reserve account opened during the year. The reduction in other mortgage assets relates to the decrease in the risk-weighting (as at March 2017) applied to the original value of the Society's self-build mortgages.

Standardised approach – exposure by asset classes and risk weights:

	Risk weight %	2017 £000	2016 £000
Cash	0	94	54
Central Banks and Government	0	58,318	41,728
Institutions	20	8,476	29,148
	50	24,982	28,035
FSRP <80% LTV	35	166,051	166,856
FSRP >80% LTV	35	671	-
	75	87	187
FSRP in arrears	100	100	502
	150	100	-
Other mortgage assets	35	2,814	-
	100	775	4,326
Fixed and other assets	20	-	67
	100	670	589
Total assets		**263,138**	**271,492**

Note: within the 35% risk weight category are £1.665million of loans and in the 100%, £0.775million of loans which are to SME's, and to which have been applied the SME factor of 76.19% available for the calculation of their risk weighting under the standardised approach, as set out in Article 501 of the Capital Requirement Regulation.

11. Operational risk:

Under the Basic Indicator Approach for operational risk, the Society calculates its average net income over the previous three years and provides 15% of that average net income as own funds requirements for operational risk.

A breakdown of the calculation of capital requirements for operational risk is provided below:

Basic Indicator Approach to Operational Risk	2017 £000	2016 £000	2015 £000
Net interest income	3,780	3,954	3,604
Other income / charges	29	31	33
Total	3,809	3,985	3,637
Basic indicator (three year average)			3,810
Own Funds Requirement (15% of the Basic Indicator)			572

Basic Indicator Approach to Operational Risk	2016 £000	2015 £000	2014 £000
Net interest income	3,800	3,958	3,567
Other income / charges	-	(1)	9
Total	3,800	3,957	3,576
Basic indicator (three year average)			3,778
Own Funds Requirement (15% of the Basic Indicator)			567

12. Leverage Ratio

Basel III introduced a non-risk based leverage ratio to supplement the risk based capital requirements. The ratio shows Tier 1 capital as a proportion of on and off balance sheet assets. The ratio does not distinguish between the credit quality of loans and acts as a primary constraint to excessive lending in proportion to the capital base. The UK leverage ratio framework requires a minimum ratio of 3.25%.

As at 31 October 2017, the Society's leverage ratio was 7.42% (2016: 6.82%) which was calculated in line with the current interpretation of the regulation as follows:

	2017	2016
	£000	£000
Total assets	263,138	271,492
Allowance for impairment	(192)	(276)
Total adjusted assets	262,946	271,216
Applicable tier 1 capital	19,525	18,493

	%	%
Leverage ratio	**7.42**	**6.82**

13. Liquidity Coverage Ratio (LCR)

The Society uses a suite of measures to monitor and manage liquidity and funding risks. One of these is the LCR which at 31 October 2017 stood at:

	2017	2016
	£000	£000
Total high quality liquid assets	58,410	41,782
Total net cash outflow	16,532	17,950
	%	%
LCR	**353.3**	**232.8**

14. Credit Risk

For a building society, credit risk is most likely to arise through the inability of borrowers to repay their mortgage commitments (mortgage credit risk) or through the failure of a treasury counterparty or country (wholesale credit risk). The Society has no appetite for material credit losses. This is controlled through credit quality standards, underwriting rules, as well as limits by exposure to counterparty, sector, country and instrument.

The Society is also exposed to credit risk through its treasury operations. This risk arises from counterparties who may be unable to repay loans and other financial instruments that the Society holds as part of its liquidity portfolio.

The counterparty limits are defined in the treasury counterparty risk policy which uses Fitch ratings agency as its External Credit Assessment Institution (ECAI). Exposure limits for individual banks on the Society's list of authorised counterparties are set taking into account Fitch's Short Term and Long Term Ratings. No bank or building society is included on the list unless it has, as a minimum, a Short Term rating of F2 and a Long Term rating of B. In addition to the use of Fitch ratings, market intelligence is used in assessing counterparty risk, in recognition that there may be a delay between a counterparty being in difficulty and this being reflected in a downgrading of its Fitch rating. A process is in place to reduce counterparty exposure limits, or to remove counterparties from the approved list, immediately without reference to the Board, but counterparties cannot be added without Board approval.

Limits are also set for diversification in terms of issuance and sector.

14.1. Concentration risk

Definition:
Concentration risk is the risk posed to a financial institution by any single or group of exposures which have the potential to produce losses large enough to threaten the ability of the institution to continue operating as a going concern.

The types of concentration risks facing the Society are concentration in one product type, geographical concentration and over-exposure to single borrowers, investors, or counterparties.

Key mitigating actions and processes:
Although the Society has only a small range of mortgage products, which are predominantly secured on residential property wholly within the UK, this concentration is of low risk because of the inherent nature of the assets and the controls in place as detailed in the lending policy.

The limit on exposure to an individual borrower or a group of connected counterparties is 10% of capital (£2.02million). The Society has no "large exposure" defined by the Building Societies Regulatory Rule Book (BSOCS) as exceeding 10% of capital as at 31 October 2017.

The Society has no dependency on any one form of introduction for mortgages and there is no concentration risk in the type of property held as security.

The Pillar 1 credit risk calculation assumes a diversified firm; therefore, additional capital is required where the Society is exposed to concentration risk.

As part of the ICAAP process, the Society quantified and provided capital for a severe economic downturn that for whatever reason affected only our core operating area. The Society accepts that Stafford and Staffordshire are its core areas and have stress tested the impact of this as part of its Pillar 2A assessment.

14.2. Mortgages:

All mortgage loan applications are assessed with reference to the Society's risk appetite and Board approved lending policy.

The Board's risk appetite is based on:

- The maximum proportion of the total mortgage portfolio that certain loans types can represent;
- Loan-to-value (LTV) ratios; and
- The arrears level.

LTV and arrears levels are key drivers of the Pillar 1 credit risk capital calculation. All mortgage products should be priced to ensure that the margin appropriately reflects the credit risk involved and the carrying cost of the incremental risk capital.

The Board believes in a stepwise approach to product development. New products should typically be introduced via a limited number of channels, such as well-established and highly reputable specialist brokers. Capital will be committed in a staged manner, with regular product performance reviews being performed.

For the Society as a whole, mortgages on prime owner occupied residential properties will be a minimum of 80% of mortgage assets and arrears rates will be kept below the national average reported by the Council of Mortgage Lenders.

The lending portfolio is monitored by the OMC to ensure that it remains in line with the stated risk appetite of the Society. All mortgage applications are manually underwritten individually on a case-by-case basis using experienced staff ensuring that they meet the lending policy rules through a full affordability assessment so supporting the risk appetite of the Society. All mortgage applications are overseen by the Mortgage Manager who ensures that all lending criteria have been applied and that all information submitted within the application is validated. As at 31 October 2017, the mortgage department consisted of the Mortgage Manager, two Business Development Managers, three staff and a secretary. All staff involved in underwriting or advising are accredited through a formal training and competence scheme. The Mortgage Manager and the Business Development Managers report to the Chief Executive.

The Society's second line Risk and Compliance function undertakes periodic reviews of the Society's lending process and the results of the reviews are reported to the Audit Committee.

The Society operates throughout England and Wales. It has no exposure to properties internationally.

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

	2017	2016
	£000	£000

On call and at short notice	217	403
In not more than three months	282	169
In more than three months but not more than one year	808	683
In more than one year but not more than five years	8,253	7,658
In more than five years	161,230	163,332
Total gross mortgages	170,790	172,245
Less: allowance for impairment	(192)	(276)
Total Net Mortgages	**170,598**	**171,969**

The maturity analysis above is based on contractual maturity not expected redemption levels.

An analysis of the Society's indexed LTV profile is shown in the table below:

	2017		2016	
LTV ratio	£000	%	£000	%
Less than 50%	84,116	49.3	76,808	44.6
51 – 70%	56,578	33.1	58,239	33.8
71 – 90%	28,607	16.8	35,345	20.5
91 – 100%	919	0.5	1,422	0.8
More than 100%	570	0.3	431	0.3
Total Gross Mortgages	**170,790**	**100.0**	**172,245**	**100.0**

Average LTV 34.8
36.0

A geographical analysis of the Society's loans and advances to members is shown below:

	2017		2016	
	£000	%	£000	%
Region:				
Stafford ST16-ST18	44,141	25.9	48,897	28.4
Rest of Staffordshire	28,564	16.7	19,816	11.5
Rest of UK	98,085	57.4	103,532	60.1
Total Gross Mortgages	**170,790**	**100.0**	**172,245**	**100.0**

During the year to 31 October 2017, the Society experienced £nil losses on mortgages (2016: £nil).

An individual FSRP provision of £13k was held at 31 October 2017 covering three residential properties as well as a collective provision on FSRP mortgages totalling £179k.

14.2. Wholesale credit risk

The purpose of the Society's ILAAP is to ensure that the Society has sufficient liquidity to meet its obligation as they fall due.

The Society's treasury risk policy is to ensure that the Society can obtain the best possible return whilst operating within prudent limits in respect of counterparties.

In accordance with its treasury counterparty risk policy, the Society only invests funds in British Government Securities, banking institutions and building societies rated at least A- as assigned by the credit rating agency, Fitch. Once a counterparty attains a rating of A, with a negative outlook,

management action is taken to reduce the exposure in that counterparty. The assets are managed with advice from external fund managers.

New limits and counterparties are considered by the ALCO before presenting recommendations to the Risk Committee for challenge and the Board for approval. The credit risk appetite for liquid assets is defined by: the minimum counterparty credit rating; the permissible instruments; the maximum percentage of total liquid assets held at each credit risk level; and the investment term. ALCO monitors exposures to counterparties and countries and ensures the Society is operating within its Board approved limits at its monthly meetings. The Board reviews the Society's exposure by sector on a monthly basis.

The maturity and credit profile of Treasury assets at 31 October 2017 is shown below:

	Maturity of Treasury Investment			
Fitch Ratings	< 3 months £000m	3 months to 1 year £000m	>1 year £000m	Total £000m
Banks: AAA to AA-	7,560	-	-	7,560
Banks: A+ to A-	4	13,345	4,623	17,972
Building Societies	1,006	7,013	-	8,019
Treasury Bills	17,420	15,472	-	32,892
British Government Securities	-	14,398	1,027	15,425
Bank of England	10,002	-	-	10,002
Total	**35,992**	**50,228**	**5,650**	**91,870**

The maturity and credit profile of Treasury assets at 31 October 2016 is shown below:

	Maturity of Treasury Investment			
Fitch Ratings	< 3 months £000m	3 months to 1 year £000m	>1 year £000m	Total £000m
Banks: AAA to AA-	13,044	8,054	2,127	23,225
Banks: A+ to A-	7,096	15,058	2,824	24,978
Building Societies	1,009	8,025	-	9,034
Treasury Bills	16,996	17,976	-	34,972
British Government Securities	2,219	4,537	-	6,756
Total	**40,364**	**53,650**	**4,951**	**98,965**

No provisions for loss relating to counterparty risk are held by the Society as at 31 October 2017.

15. Analysis of Past Dues

The Society's current lending policy is in accordance with its risk appetite, which has been established by the Board, and has produced an inherently low risk mortgage book. The Society has strong management controls over arrears with no losses arising from default leading to possession in the year to 31 October 2017. The average loan to value of the residential mortgage book was 34.8% as at 31 October 2017.

The table below provides information on mortgage loans by payment due status:

	2017		2016	
	£000	%	£000	%

Not impaired:				
Neither past due nor impaired	167,139	98.0	166,467	96.8
Past due up to three months but not impaired	3,265	1.9	4,954	2.9
Past due over three months but not impaired	113	0.1	532	0.3
Possessions	-	-	-	-
Impaired:				
Past due up to three months	174	0.1	292	0.2
Past due over three months	-	-	-	-
Possessions	99	-	-	-
Total gross mortgages	170,790		172,245	
Allowance for impairment	(192)	(0.1)	(276)	(0.2)
Total Net Mortgages	**170,598**	**100.0**	**171,969**	**100.0**

A table of the Society's "past due" loans by geographical area, which are loans more than 90 days in arrears, as at 31 October 2017 is set out below:

	Residential loans		Commercial loans		
Region	Past due	Performing	Past due	Performing	Total
	£m	£m	£m	£m	£m
Stafford ST16 – ST18	-	42.5	-	1.6	44.1
Rest of Staffordshire	0.1	27.8	-	0.7	28.6
Rest of UK	0.1	97.7	-	0.3	98.1
Total Gross Mortgages	**0.2**	**168.0**	**-**	**2.6**	**170.8**

The table of the Society's "past due" loans by geographical area, which are loans more than 90 days in arrears, as at 31 October 2016 is set out below:

	Residential loans		Commercial loans		
Region	Past due	Performing	Past due	Performing	Total
	£m	£m	£m	£m	£m
Stafford ST16 – ST18	0.1	47.0	-	1.8	48.9
Rest of Staffordshire	0.2	18.9	-	0.7	19.8
Rest of England	0.2	102.9	-	0.3	103.4
Scotland	-	0.1	-	-	0.1
Total Gross Mortgages	**0.5**	**168.9**	**-**	**2.8**	**172.2**

16. Provisions

The Society's allowance for impairment is set out below:

	Loans fully secured on Residential Property		Loans fully secured on Land		
	Individual	Collective	Individual	Collective	Total
	£000	£000	£000	£000	£000
Balance at 1 November 2016	3	273	-	-	276
Charge/(credit) for the year	10	(94)	-	-	(84)
Balance at 31 October 2017	**13**	**179**	**-**	**-**	**192**

Provisions on commercial and residential accounts are made to reduce the value of loans and advances to the amount that is considered likely to be ultimately recoverable in the event of the relevant property held as security being sold in possession by the Society.

The Society considers evidence of impairment for loans and advances at both a specific asset and a collective level. All individually significant loans and advances are assessed for specific impairment. Those found not to be specifically impaired are then collectively assessed for any impairment that has been incurred but not yet identified. Loans and advances that are not individually significant are collectively assessed for impairment by grouping together loans and advances with similar risk characteristics.

In assessing collective impairment, the Society uses statistical modelling of historical trends of the probability of default, the timing of recoveries and the amount of loss incurred, and makes an adjustment if current economic and credit conditions are such that the actual losses are likely to be greater or lesser than is suggested by historical trends. Default rates, loss rates and the expected timing of future recoveries are regularly benchmarked against actual outcomes to ensure that they remain appropriate.

Where certain emerging impairment characteristics are considered significant but not assessed as part of the impairment calculation, the Board may elect to apply an overlay to the impairment provision.

The amount of impairment loss is recognised immediately through the income statement and a corresponding reduction in the value of the financial asset is recognised using provisions.

- In determining whether an impairment loss should be recorded, the Society is required to exercise a degree of judgement. Impairments are calculated as the difference between expected future cash flows and the current outstanding balance, using management's best estimate of propensity to default using all available data. Estimates and assumptions are around the probability of any account going into default, the probability of defaulting accounts progressing to possession, the time taken to complete the sale of properties in possession and the eventual loss incurred in the event of forced sale or write-off. These assumptions are based on observable historical data and updated as management considers appropriate to reflect current circumstances. A 5% increase in the outcome of probability of default or eventual loss incurred would result in an increase in the impairments of £2, 000.

17. Market Risk and Interest Rate Risk in the Banking Book (IRRBB)

Market risk is the risk that the value of, or income arising from, the Society's assets and liabilities changes as a result of changes in market prices, the principal elements being interest rate risk, foreign currency risk and equity risk.

The Society only deals with products in sterling so is not directly affected by currency risk. The Society's products are also only interest orientated products so are not exposed to other pricing risks.

IRRBB is the impact on economic value due to movements in interest rates and arises from mismatches of the re-pricing or maturity of assets and liabilities as interest rates change. The Society has a relatively simple treasury structure, with the majority of mortgages and all savings products currently on administered rates, while liquidity is typically of short duration. As a result, interest rate risk for the Society is significantly less than for other institutions.

The Society's main exposure to interest rates arises from its investment in Government Gilts and Certificates of Deposit with other financial institutions.

Static gap analysis is performed monthly against a 2% parallel shift in interest rates (given the current base rate of 0.50%, the Society has stress tested downwards against a fall of 0.50% in interest rates). ALCO monitors gap reports monthly and the effect of a shift in interest rates as a percentage of capital and reports to the Risk Committee.

The results of the stress test at 31 October 2017 are as follows:

	Impact on net interest income £000 £000
Impact of interest rate shift of +2%	682
Impact of interest rate shift of -0.50%	173

The results of the stress test at 31 October 2016 were as follows:

	Impact on net interest income £000
Impact of interest rate shift of +2%	636
Impact of interest rate shift of -0.25%	80

18. Remuneration and Material Risk Takers

The Society complies with the principles in the UK Corporate Governance Code 2016 relating to remuneration as far as they are applicable to a mutual organisation of the Society's size. The remuneration policy complies with the relevant elements of the FCA's Remuneration Code.

Full details of the Society's remuneration policy and details of Executive Directors' emoluments for 2017 and comparatives for 2016 are set out in the Directors' Remuneration Report to the Annual Report and Accounts, available on the Society's website, which should be read in conjunction with this report.

The Society's objective in setting remuneration policies is to ensure that they are in line with its business strategy, risk appetite and long-term objectives, and that remuneration is set at a level that retains and attracts staff of the appropriate calibre.

Remuneration of Executive Directors and the Risk and Compliance Manager is determined by the Remuneration Committee, which consists of all the Non-Executive Directors chaired by Mrs Karen McCormick. In setting remuneration, the Committee takes account of fees, salaries and other benefits provided to Directors and to other senior management of comparable institutions. Non-Executive Directors are paid fixed fees only. The remuneration of the MLRO, in common with all other staff, is set by the Chief Executive, subject to overall budgetary controls set by the Board during producing the Society's Corporate Plan.

A bonus is paid to the Executive Directors. The bonus is assessed by the Remuneration Committee and is based on a range of financial and non-financial corporate performance targets. Bonus payments are payable annually, are not guaranteed and are reviewed each year.

No Executive Director holds a contract with a notice period of more than twelve months.

18.1. Remuneration Code Staff

Code staff are defined by the Financial Conduct Authority (FCA) as "staff that have a material impact on the firm's risk profile; this includes staff that perform significant influence functions, senior managers and risk takers".

The Board has determined that Non-Executive Directors, Executive Directors, the Risk and Compliance Manager, the MLRO other key management and staff whose duties require them to have a relevant qualification fall within the definition of Remuneration Code staff under SYSC 19D of the PRA Handbook. These staff are now identified as “Material Risk Takers” under CRD IV.

Information concerning the mandate of the Remuneration Committee and the decision-making process it uses in determining remuneration policy is contained within the terms of reference which are available on the Society’s website.

Aggregate information on Remuneration Code Staff during the years ending 31 October 2017 and 31 October 2016 is given below:

	2017				2016	
	Number	Fixed Remuneration £000	Variable Remuneration £000	Total Remuneration £000	Number	Total Remuneration £000
Non-Executive Directors	7	124	0	124	7	116
Executive Directors	3	246	28	274	2	247
Other Remuneration Code staff	12	459	5	464	2	102

Since last year, staff who qualify under the qualitative criteria of the Regulatory Technical Standard supporting the Remuneration Code have been added to the list of Material Risk Takers, which previously only included those with Prudential Regulatory Authority Senior Management Functions.

Fixed Remuneration for Other Remuneration Code Staff includes pension contributions paid by the Society. No other benefits are paid and Directors do not receive pension contributions from the Society.

19. Glossary

Arrears:
A customer is in arrears when they are behind in meeting their contractual obligations with the result that an outstanding loan payment is overdue. The value of the arrears is the value of any payments that have been missed.

Basel II:
Basel II is the second of the Basel Accords, issued by the Basel Committee on Banking Supervision, which defines the methods by which firms should calculate their regulatory capital requirements to retain sufficient capital to protect the financial system against unexpected losses. Basel II became law in the EU Capital Requirements Directive, and was implemented in the UK via the PRA/FCA Handbook.

Basel III:
Basel III became effective in the UK on 1 January 2014 through CRD IV and sets out the details of strengthened global regulatory standards on bank capital adequacy and liquidity.

Capital Requirements Directive (CRD IV):
CRD IV is the European legislation which came into force from 1 January 2014 to implement Basel III. It is made up of the Capital Requirements Regulation (CRR) and the Capital Requirements Directive (CRD), outlining the capital requirements framework and introduced liquidity requirements, which regulators use when supervising firms.

Common Equity Tier 1 capital (CET1):
CET1 capital consists of internally generated capital generated from retained profits, other reserves less intangible assets and other regulatory deductions. CET1 capital is fully loss absorbing.

Common Equity Tier 1 ratio:
Common Equity Tier 1 capital as a percentage of risk weighted assets.

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

Credit Quality Steps:
A credit quality assessment scale as set out in CRR Articles 111 - 141 (Risk weights under the Standardised Approach to credit risk).

Credit risk:
This is the risk that a customer or counterparty fails to meet their contractual obligations.

Debt securities:
Assets representing certificates of indebtedness of credit institutions, public bodies or other undertakings excluding those issued by central banks.

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

Fair value:
Fair value is the amount for which an asset could be exchanged or a liability settled, between knowledgeable, willing parties in an arm's length transaction.

Financial Conduct Authority (FCA):
The statutory body responsible for conduct of business regulation and supervision of UK authorised firms.

Impairment:
The term impairment is usually associated with a long-lived asset that has a fair market value less than the historical cost (or book value) of the asset.

Impaired loans:
Loans where there is objective evidence that an impairment event has occurred, meaning that the Society does not expect to collect all the contractual cash flows or expect to collect them later than they are contractually due. Impaired loans are defined as those which are more than three months in arrears or in possession. However other indicators of impairment may result in provisioning for losses.

Interest Rate Risk:
The risk of loss of income from movements in interest rates in severe but plausible market rate movements.

Internal Capital Adequacy Assessment Process ICAAP):
The Society's own assessment of the levels of capital that it needs to hold in respect of its regulatory capital requirements for risks it faces under a business as usual scenario including stress events.

Individual Liquidity Adequacy Assessment Process (ILAAP):
The Society's own assessment of the liquidity resources it requires in order to remain within the risk tolerances it has set. This will include an evaluation of potential stresses based on multiple market environments.

Institutions:

Financial institutions such as banks and building societies.

Leverage Ratio:
The ratio of Tier 1 capital divided by the total exposures which includes on and off-balance sheet items.

Loan to value (LTV):
LTV expresses the amount of a mortgage as a percentage of the value of the property.

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

Operational risk:
The risk of loss arising from inadequate or failed internal processes, people and systems, or from external events.

Other items:
Other assets not included in other definitions.

Past due items:
Loans which are 90 days or more in arrears.

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

Prudential Regulation Authority (PRA):
The statutory body responsible for the prudential supervision of banks, building societies, insurers and small number of significant investment firms in the UK. The PRA is a subsidiary of the Bank of England.

Risk appetite:
The articulation of the level of risk that the Society is willing to accept (or not accept) in order to safeguard the interests of the Society's members whilst achieving business objectives.

Risk weighted assets (RWA):
The value of assets, after adjustment, under the relevant Basel III capital rules to reflect the degree of risk they represent.

Secured by Mortgages on Commercial Real Estate:
Secured business lending which is only made available to small and medium-sized enterprises.

Standardised Approach:
The basic method used to calculate capital requirements for credit risk. In this approach the risk weightings used in the capital calculation are determined by specified percentages.

Tier 1 capital:
A component of regulatory capital, it comprises CET1.

Tier 2 capital:
Comprises the collective impairment allowance (for exposures treated on a Standardised basis), less certain regulatory deductions.

Tier 1 ratio:
Tier 1 capital as a percentage of risk weighted assets.

Appendix To Pillar 3 Disclosure Document For The Year Ended 31 October 2017
Template 1: Overview Of Risk Weighted Assets (RWA)

		RWA		Minimum capital requirements
		2017 £000	**2016 £000**	**2017 £000**
1	Credit risk (excluding counterparty credit risk)	14,186	19,848	1,135
2	Of which: standardised approach (SA)	14,186	19,848	1,135
3	Of which: foundation internal ratings-based (F-IRB) approach			
4	Of which: supervisory slotting approach			
5	Of which: advanced internal ratings-based (A-IRB) approach			
6	Counterparty credit risk (CCR)	60,160	63,368	4,813
7	Of which: standardised approach for counterparty credit risk	60,160	63,368	4,813
8	Of which: Internal Model Method (IMM)			
9	Of which: other CCR			
10	Credit valuation adjustment (CVA)			
11	Equity positions under the simple risk weight approach			
12	Equity investments in funds – look-through approach			
13	Equity investments in funds – mandate-based approach			
14	Equity investments in funds – fall-back approach			
15	Settlement risk			
16	Securitisation exposures in banking book			
17	Of which: securitisation external ratings-based approach (SEC-IRBA)			
18	Of which: securitisation external ratings-based approach (SEC-ERBA), including internal assessment approach (IAA)			
19	Of which: securitisation standardised approach (SEC-SA)			
20	Market risk			
21	Of which: standardised approach (SA)			
22	Of which: internal model approaches (IMA)			
23	Capital charge for switch between trading book and banking book			
24	Operational risk	7,144	7,083	572
25	Amounts below the thresholds for deduction (subject to 250% risk weight)			
26	Floor adjustment			
27	Total (1+6+10+11+12+13+14+15+16+20+23+24+25+26)	81,490	90,299	6,520

Note that the £53k difference between minimum capital requirements here and that on page 14 of the Pillar 3 Disclosure Document relates to "fixed and other assets".

The primary differences in the 2017 risk weighted asset compared to 2016 relate to:

- Credit risk: the elimination of exposures to overseas counterparties to accord with the Administered Approach to treasury management and usage of the Bank of England reserve account.
- Counterparty credit risk: this relates to the decrease in the risk-weight (as at March 2017) applied to the original value of the Society's self-build mortgages.

Template 2: Leverage Ratio

Summary comparison of accounting assets vs leverage ratio exposure measure

		2017 £000
1	Total consolidated assets as per published financial statements	263,138
2	Adjustment for investments in banking, financial, insurance or commercial entities that are consolidated for accounting purposes but outside the scope of regulatory consolidation	
3	Adjustment for fiduciary assets recognised on the balance sheet pursuant to the operative accounting framework but excluded from the leverage ratio exposure measure	
4	Adjustments for derivative financial instruments	
5	Adjustment for securities financing transactions (I.e. repos and similar secured lending)	
6	Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	
7	Other adjustments	(192)
8	**Leverage ratio exposure measure**	**262,946**

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Template 3: Leverage Ratio Common Disclosure Template

		2017 £000	2016 £000
On-balance sheet exposures			
1	On-balance sheet exposures (excluding derivatives and securities financing transactions (SFTs), but including collateral	263,138	271,492
2	(Asset amounts deducted in determining Basel III Tier 1 capital)	(192)	(276)
3	**Total on-balance sheet exposures (excluding derivatives and SFTs) (sum of rows 1 and 2)**	262,946	271,216
Derivative exposures			
4	Replacement cost associated with all derivatives transactions (where applicable net of eligible cash variation margin and/or with bilateral netting)		
5	Add-on amounts for PFE associated with all derivatives transactions		
6	Gross-up for derivatives collateral provided where deducted from the balance sheet assets pursuant to the operative accounting framework		
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)		
8	(Exempted CCP leg of client-cleared trade exposures)		
9	Adjusted effective notional amount of written credit derivatives		
10	(Adjusted effective notional offsets and add-on deductions for written credit derivatives)		
11	**Total derivative exposures (sum of rows 4-10)**		
Securities financing transaction exposures			
12	Gross SFT assets (with no recognition of netting), after adjusting for sale accounting transactions		
13	(Netted amounts of cash payables and cash receivables of gross SFT assets)		
14	CCR exposure for SFT assets		
15	Agent transaction exposures		
16	**Total securities financing transaction exposures (sum of rows 12 – 15)**		
Other off-balance sheet exposures			
17	Off-balance sheet exposure at gross national amount		
188	(Adjustments for conversion to credit equivalent amounts)		
19	**Off-balance sheet items (sum of rows 17 and 18)**		
Capital and total exposures			
20	Tier 1 capital	19,525	18,493
21	Total exposures (sum of rows 3,11,16 and 19)	262,946	271,216
Leverage ratio			
22	**Basel III leverage ratio**	7.42%	6.82%

Definitions and Instructions

SFTs: transactions such as repurchase agreements, reverse repurchase agreements, security lending and borrowing, and margin lending transactions, where the value of the transactions depends on market valuations and the transactions are often subject to margin agreements.

Template 4: Liquidity Coverage Ratio (LCR)

		Total unweighted value (average) £000	Total weighted value (average) £000
High-quality liquid assets			
1	Total HQLA		58,410
Cash outflows			
2	**Retail deposits and deposits from small business customers, of which:**	234,580	13,973
3	Stable deposits	198,089	9,904
4	Less stable deposits	36,491	4,069
5	**Unsecured wholesale funding, of which:**	7,463	2,900
6	Operational deposits (all counterparties) and deposits in networks of cooperative banks		
7	Non-operational deposits (all counterparties)	7,463	2,900
8	Unsecured debt		
9	**Secured wholesale funding**		
10	**Additional requirements, of which:**	8,415	1,749
11	Outflows related to derivative exposures and other collateral requirements		
12	Outflows related to loss of funding on debt products		
13	Credit and liquidity facilities	8,415	1,749
14	**Other contractual funding obligations**	252	
15	**Other contingent funding obligations**		
16	**TOTAL CASH OUTFLOWS**		18,622
Cash inflows			
17	**Secured lending (e.g. reverse repos)**		
18	**Inflows from fully performing exposures**	1,027	596
19	Other cash inflows	7,470	1,494
20	**TOTAL CASH INFLOWS**	8,497	2,090
			Total adjusted value
21	**Total HQLA**		58,410
22	**Total net cash outflows**		16,532
23	**Liquidity Coverage Ratio (%)**		353.3%