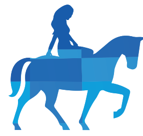
COVENTRY
Building Society



Pillar 3 Disclosures

For the year ended 31 December 2021

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1. Introduction

In this document Coventry Building Society (the Society) has in accordance with Part 8 of the Capital Requirements Regulation (CRR) set out its Pillar 3 disclosures. These disclosures cover:

- the Society's Risk Management Strategy including details of the management, mitigation, monitoring, measuring and reporting of risks at the Society;
- the Society's Capital Position and the risks that affect that position; and
- the Society's Liquidity Position and the risks that affect that position.

The document should be read in conjunction with the Coventry Building Society Annual Report & Accounts for the year ending 31 December 2021 (Accounts). These disclosures have been approved by the Board Audit Committee (BAC) on behalf of the Board. These disclosures have not been, and are not required to be, subject to independent external audit, and do not constitute any part of the Society's financial statements.

	Transitional[1]		End-point	
	2021 £m	2020 £m	**2021 £m**	2020 £m
Available own funds (amounts)				
Common Equity Tier 1 (CET 1) capital	**1,924.2**	1,783.7	**1,921.8**	1,783.3
Tier 1 capital	**2,355.2**	2,230.7	**2,336.8**	2,198.3
Total capital	**2,360.7**	2,241.8	**2,336.8**	2,198.3
Risk-weighted assets (amounts)				
Total risk-weighted assets	**5,305.5**	5,410.9	**5,303.6**	5,410.6
Risk- based capital ratios as a percentage of RWA				
Common Equity Tier 1 ratio (%)	**36.3%**	33.0%	**36.2%**	33.0%
Tier 1 ratio (%)	**44.4%**	41.2%	**44.1%**	40.6%
Total capital ratio (%)	**44.5%**	41.4%	**44.1%**	40.6%
Additional CET 1 buffer requirements as a percentage of RWA				
Capital conservation buffer (%)	**2.5%**	2.5%	**2.5%**	2.5%
Countercyclical capital buffer (%)	**0.0%**	0.0%	**0.0%**	0.0%
Total of CET 1 specific buffer requirements (%)	**2.5%**	2.5%	**2.5%**	2.5%
CET 1 available after meeting minimum capital requirements, but before buffer requirements (%)	**31.8%**	28.5%	**31.7%**	28.5%
UK Leverage ratio				
UK leverage ratio exposure measure	**48,471.7**	46,480.0	**48,471.7**	46,480.0
UK leverage ratio (%)	**4.8%**	4.6%	**4.8%**	4.6%
CRR Leverage ratio				
CRR leverage ratio exposure measure	**54,799.3**	51,688.2	**54,799.3**	51,688.2
CRR leverage ratio (%)	**4.3%**	4.3%	**4.3%**	4.3%
Liquidity coverage ratio[2]				
Total HQLA	**6,884.8**	5,888.3	**6,884.8**	5,888.3
Total net cash outflows	**3,765.6**	2,880.8	**3,765.6**	2,880.8
Liquidity coverage ratio (%)	**182.6%**	205.5%	**182.6%**	205.5%

Table 1 Key metrics

Notes

1. Transitional figures take account of capital regulations that are subject to transitional periods. For the Society, this means the inclusion of a portion of otherwise ineligible "grandfathered" capital and IFRS9 relief.

2. The Liquidity Coverage data in the key metrics table are calculated on a 12-month average basis.

1.1. Background

This Pillar 3 document sets out disclosure requirements under the Capital Requirements Regulation (CRR) and Capital Requirements Directive IV (CRD IV[1]). These are known as Pillar 3 disclosures because they complement the minimum capital requirements in Pillar 1 and the supervisory review process in Pillar 2. The Pillar 3 disclosures are aimed at promoting market discipline by providing information on risk exposures and the management of those risks.

CRD IV requires a concise risk statement approved by the management body which describes the institution's overall risk profile associated with its business strategy. This is evidenced by its simple business model and prudent lending policy with a conservative balance weighted indexed loan to value (LTV) of 50.9% (2020: 52.8%) and low levels of historic arrears. While arrears have been impacted by borrowers' ability to meet payments against the economic backdrop of Covid-19 and increased slightly in 2021, as at 31 December 2021 only 0.10% of mortgage balances were 2.5% or more in arrears (2020: 0.09%) compared to the latest available industry average of 0.67%[2]. The Society's Common Equity Tier 1 capital ratio was 36.2% at 31 December 2021 (2020: 33.0%). Additional information on the risks the Society is exposed to and how it manages these risks is included in this document and also within the Risk Management Report in the 2021 Accounts which is published on the Society's website (www.coventrybuildingsociety.co.uk).

1.2. Policy and frequency of disclosures

The Board has adopted a formal policy to comply with Pillar 3 disclosure requirements outlined in Article 431 (3).

In accordance with Article 432 of the CRR no disclosures have been omitted as either being proprietary or confidential. The only omissions on materiality grounds relate to those which would be disclosed under Article 447 'Exposures in equities not included in the trading book'. The fair value of these investments is £4.9 million (0.01% of the Society's total assets) and they are made up of shares in Visa Inc. Further information on these investments can be found in the 2021 Accounts which is published on the Society's website (www.coventrybuildingsociety.co.uk).

In accordance with Article 433 of the CRR, the Society publishes disclosures on an annual basis. The Society closely monitors the regulatory environment to ensure continued compliance with upcoming changes.

1.3. Verification

These disclosures have been approved by the BAC on behalf of the Board. These disclosures have not been, and are not required to be, subject to independent external audit, and do not constitute any part of the Society's financial statements.

1.4. Governance arrangements and remuneration

Disclosure requirements relating to governance arrangements under Article 435 of the CRR, and in particular the declaration approved by the Board of the adequacy of risk management arrangements, are included in the Directors' Report on Corporate Governance and Annual Business Statement within the 2021 Accounts published on the Society's website (www.coventrybuildingsociety.co.uk).

The disclosures required under Article 450 of the CRR and the Prudential Regulation Authority's (PRA) Remuneration rules are included in the Directors' Remuneration Report within the 2021 Accounts.

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[1] On 28 December 2020 the PRA published PS29/20 which implemented elements of CRD V. However, some amendments related to UK regulation only apply from 31 December 2021.

[2] Source: Bank of England.

1.5. Scope of disclosures

The Society is a UK parent institution that is regulated by the PRA and Financial Conduct Authority (FCA) and is not a Globally or Other Systemically Important Institution. The CRD IV framework applies to the Society and its subsidiary undertakings. Information on these subsidiaries is set out in the 2021 Accounts. There are no differences between the basis of consolidation of the Group for accounting and CRD IV purposes in preparing the Pillar 3 disclosures.

Regulatory capital ratios are calculated on both a UK Consolidation Group and an Individual Consolidated (or solo-consolidated) basis. The subsidiaries included in the Individual Consolidated basis are Godiva Mortgages Limited and ITL Mortgages Limited.

The Society does not foresee any practical or legal impediments to the transfer of capital resources or the repayment of liabilities between the Society and the entities included in the Individual Consolidated basis.

The Group consolidation also includes structured entities used by the Society in its wholesale funding programmes. These entities have minimal levels of retained capital and risk weighted assets. As a result there are no significant differences between the Individual Consolidated basis and the Group. For this reason, the disclosures in this document are made on a Group basis only and the term Society is used as a reference for the Group.

2. Risk management policies and objectives

2.1. Overview

The Society is a mutual organisation run for the long-term benefit of its members. In keeping with this, the Board adopts a prudent approach to managing risk.

2.2. Top and emerging risks

Risk	Mitigation
Macroeconomic environment The economic outlook remains uncertain and the medium term impacts of the pandemic and exit from the European Union may still impact economic activity. Supply chain issues, inflationary pressure and a difficult environment for businesses to hire workers may contribute to this.	The Society performs regular stress testing considering the impact of severe economic downturns and confirms that we expect to withstand severe stresses. The Society's lower risk lending approach, for example using higher affordability stress rates, means that our arrears level remains well below industry levels.
Market environment A reduction in mortgage activity combined with a more volatile interest rate environment could put continued downward pressure on mortgage margins and restrict opportunities for growth relative to other firms.	The Society's simple, lower risk and lower cost business model means that it is well placed to maintain flexibility and strength through a range of market conditions. The Society undertakes a detailed Strategic Plan process which ensures the needs of savings and borrowing members is balanced with the strength and resilience of the Society.
Changing customer behaviour and expectations Customer expectations and increased use of digital channels are changing the way that savings and mortgage products are designed and delivered. This has accelerated since the pandemic and associated social distancing measures. There is a risk that the Society's products do not keep up with the pace of change, or that the requirements challenge the Society's low cost operating model.	The Society continues to focus on developing products and services which keep up with the change in demand and we are increasing our investment in digital servicing and distribution throughout the Strategic Plan period. Our plan includes the requirement for both short-term change and long-term strategic investment.
Technology and innovation There is a risk that the level of investment in technology and innovation could fall behind others in our core markets, reducing the Society's attractiveness to customers, or that the change activity itself could impact service levels, growth or other performance measures.	The Society's new product-based change model is expected to improve resilience, flexibility and efficiency of delivering technology and other change.
Operational resilience A major operational risk event could result in disruption to services leading to customer harm, financial or regulatory impacts or to reputational damage. Such	The Society manages risk through its Enterprise Risk Management Framework (ERMF) and its response to risk events is tested regularly. This is supported by progress against the regulatory requirements on operational resilience which aim

events could include the increasing threat of cyber attacks, loss of data or service outages. The Society may not be able to attract and retain people with the skills and knowledge to sustain its operational resilience.	to ensure that the Society's key services are able to recover in a timely manner in the event of disruption.
Regulatory environment There is a risk that the scope and complexity of regulatory changes arising from both the PRA and the FCA could increase the Society's costs and funding requirements.	The Society conducts horizon scanning and engages with trade bodies and its regulators constructively to ensure the impact of regulation on its business model is managed closely.
Climate change The risks of climate change could create material disruption to the Society's business as a result of transition risk as the UK economy transitions to lower carbon activities. This includes the potential impact of new regulations in our core markets.	The Society has enhanced its understanding of climate risk and its impact on the business model. The continued focus on understanding and planning for the impact of climate change is recognised in the Society's Strategic Plan and Sustainability Report.

Table 2 Top and emerging risks

2.3. Principal risks

The principal risk categories to which our business model is inherently exposed are set out below. These risks are managed through the Society's Enterprise Risk Management Framework (ERMF); more information on these risks is included within this report.

Principal risks are those risks that the Society believes could significantly affect the achievement of the Society's purpose. Additionally, top and emerging risks, those risks that could impact the Society's Strategic plan or business model, are regularly considered and reviewed.

Information on the Society's top and emerging risks is included in the 2021 Accounts.

As a UK building society there are a number of principal risks that the Society is inherently exposed to. These risk categories are summarised below, in addition to information on how the Society mitigates and manages them.

Principal risks	Mitigation
Retail credit risk The risk of loss to the Society if borrowers do not meet their contractual payments in full and/or on time.	We operate robust underwriting and affordability assessments which, together with appropriate credit policies, results in the Society lending responsibly and remaining low risk.
Treasury credit risk The risk that the Society's wholesale creditors are unable to meet their financial obligations or that the underlying value of the wholesale asset suffers due to changes in creditworthiness of the counterparty.	We operate under a treasury risk management framework reviewed annually by the Board which limits the size and breadth of exposures to good quality counterparties with a low risk of failure.

Market risk The risk of a reduction in earnings and/or value as a result of financial market movements.	We operate within Board approved limits and use interest and foreign exchange rate swap agreements to mitigate the impact of changes in interest rates and foreign exchange rate.
Liquidity and funding risk The risk of insufficient funds to meet obligations falling due or the inability to access funding at reasonable cost or risk.	We hold sufficient liquidity to withstand a severe but plausible stress and operate within limits set by the Board. We maintain a diversified funding base to avoid any overreliance on any funding source, type or term.
Conduct risk The risk that the Society's activities fail to deliver good customer outcomes.	We place good customer outcomes at the heart of our decision making. In line with Putting Members First, this reduces conduct risk. This ethos is embedded in product design, services, and people and communication strategies.
Operational risk The risk of loss arising from inadequate internal processes, people and systems, or from external events, Such events could include the increasing threat of cyber attacks, loss of data or service outages. This includes both legal and regulatory risk.	We actively identify, assess and manage the operational risks to which the Society is exposed. During 2021 we continued to adapt, enhancing our operational risk management framework to enable the Society to react effectively to the demands of the Covid-19 pandemic, as well as ongoing regulatory requirements and change. We have built in business continuity capability and have undertaken work to understand the key services to ensure operational resilience. We closely monitor the regulatory environment to understand and model the impact of upcoming regulatory change.
Model risk The risk of an ineffective or incorrectly interpreted model leads to losses, reputational damage or regulatory censure.	We operate robust model governance protocols including sensitivity analysis on key assumptions, independent model validation and regular model monitoring. We are enhancing our approach to data governance.
Strategic risk The risk that the business model or strategy becomes inappropriate given changes to macroeconomic, geopolitical, regulatory (including climate change) or other factors (including changing customer behaviour and expectations in an increasingly digital world).	We have a simple business model which focuses on well-understood risks and opportunities. We have a robust strategic planning process which includes capital and liquidity stress testing. The strategic planning assumptions are regularly reviewed to ensure there continues to be focus on risks which could become threats to the business model over the medium to long term.

Table 3 Principal risks

The Society also has a level of pension obligation risk (i.e. the risk that, as the sponsor of the Society's pension scheme, the Society is exposed to adverse movements in the actuarial valuation of the fund) in relation to the now closed defined benefit pension scheme. The Society continues to monitor the pension scheme to ensure that there is no scheme deficit over the medium term and details on the Society's management of pension obligation risk are provided in the 2021 Accounts.

Disclosures relating to market, conduct, and strategic risks (including climate change) are included in the Risk Management Report in the 2021 Accounts and are not duplicated in this document. Disclosures for liquidity and funding, operational and model risk are included within this document with additional information included in the 2021 Accounts. The required Asset Encumbrance disclosures are included in Appendix 3 and Liquidity Coverage Ratio (LCR) disclosures in Appendix 7. This document does, however, include additional credit risk information to that in the 2021 Accounts given that credit risk is the principal driver of the Society's Pillar 1 capital requirement. In order to provide the reader with a comprehensive overview of credit risk, the 2021 Accounts disclosures on credit risk are also included in this document.

2.4. Controlling and managing risk - overview

The Society operates a simple business model. It manages risk through the ERMF, which sets out the Board's approach to managing and overseeing risk by; defining risk strategy, risk appetite, governance and control, and risk management in light of the Society's strategy.

The ERMF is approved annually by the Board to ensure it operates effectively. The Society will continue to enhance the ERMF as required to ensure it identifies and manages risk within its low risk appetite.

2.5. Risk strategy

The Board sets the Society's risk strategy and risk management approach. The strategy includes establishing a robust risk culture, setting the Board's risk appetite and ensuring that the 'three lines of defence' model operates effectively.

2.6. Risk culture

Risk culture is reflected in the behaviour and approach of the Board and all employees to risk awareness, risk taking and risk management. A strong risk culture helps the Society to achieve its strategy within acceptable risk levels.

The Society's risk culture is built on the following four elements:

1. Tone from above – the Board and executive management act, and encourage employees to act, with openness and integrity, especially in the fair treatment and duty to members. Employees are encouraged to report observed non-compliance, risk incidents and 'near misses'.
2. Accountability – employees understand both the core values of the Society and its approach to risk. Where individuals have specific risk management responsibilities, these are included within role profiles and objectives, and employees understand that they will be held accountable for their actions and risk taking behaviours. Substantially all Society roles are covered by the 'Strengthening Accountability in Banking' regulatory framework, which sets standards for those working within financial services.
3. Effective communication and challenge – a sound risk culture should promote an environment of open communication and effective challenge in which decision making processes encourage a broad range of views, allow for testing of current practices, stimulate a constructive critical attitude among colleagues, and promote an environment of open and constructive engagement throughout the Society. The Society has embedded an enhanced and effective Whistleblowing policy with supporting procedures.
4. Incentives – the Society makes sure that its performance management and reward frameworks are effectively designed and embedded to promote its desired risk management behaviours and attitudes.

In particular, the Society does not pay any sales incentives to employees.

The Society undertook a risk culture review during 2021 with the results reported to the Board Risk Committee (BRC). The review concluded there is a strong risk culture embedded across the Society.

2.7. Board risk appetite

The Board articulates the risks it is willing to take in delivering the Strategic Plan through its risk appetite statements which create a framework for decision making. These appetite statements are reviewed on an annual basis to ensure they remain effective.

The Board's strategy towards risk and risk appetite is to achieve operational, conduct and prudential resilience that protects the long-term interests of our membership and the Society, and also reflects our market role in supporting economic growth and financial stability.

Boundary conditions have been developed and calibrated in order to help achieve this. Where management can meet strategic objectives without using the full extent of the Society's risk appetite, the Board expects it to do so.

The Executive Risk Committee (ERC), the BRC and the Board all review performance and adherence to Board limits.

2.8. Three lines of defence

The Society operates within a 'three lines of defence' model, recognised as an industry standard for risk management. The key accountabilities of the three lines of defence within the Society are set out below:

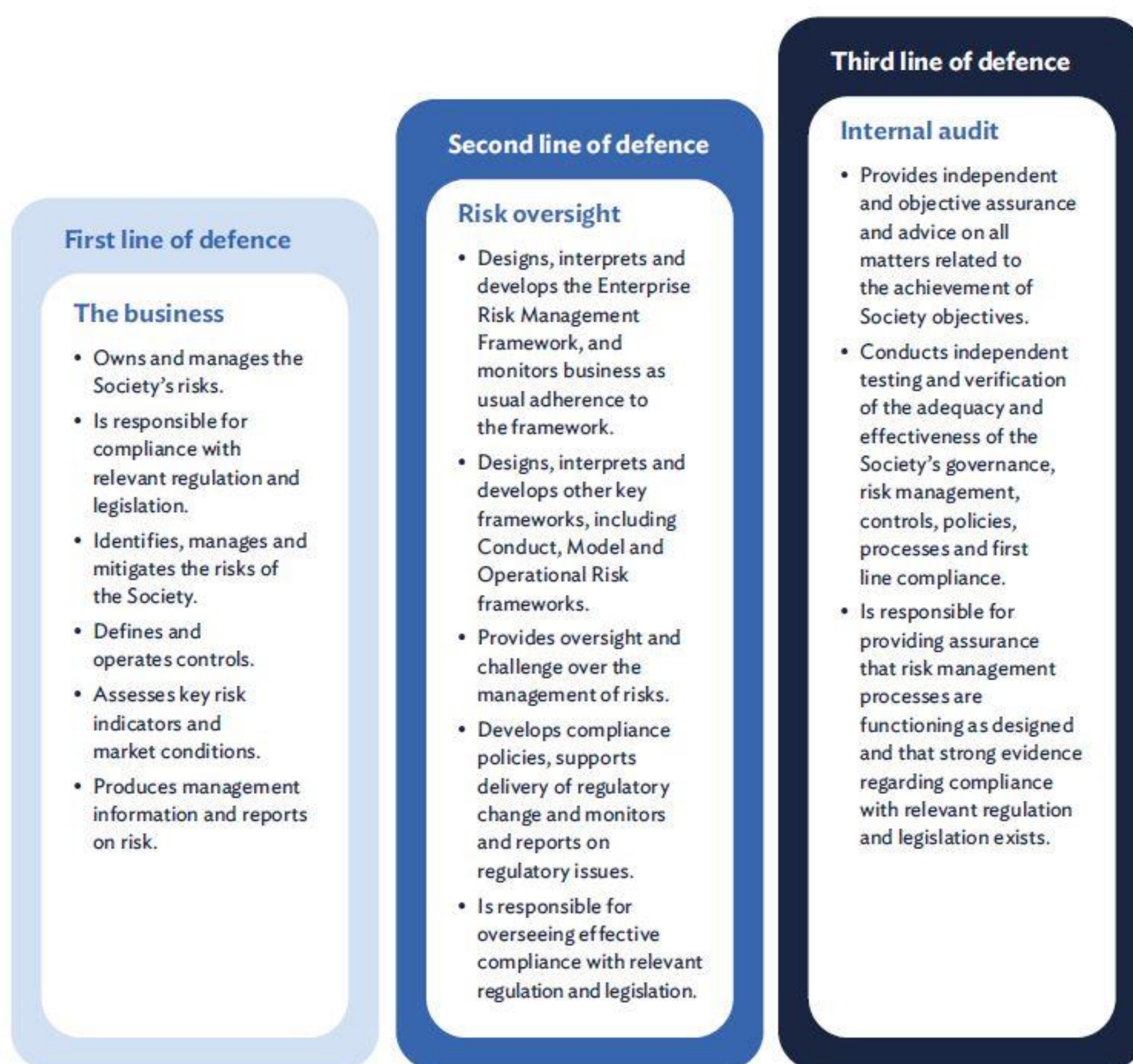

Figure 1 Three lines of defence

2.9. Governance and control

The Society has a number of committees which oversee and monitor risk as set out below. The Board delegates to BRC oversight of the Society's risk management arrangements as a whole. The Chief Risk Officer (CRO) has an independent reporting line directly to the Chair of the BRC in addition to reporting to the Chief Executive.

The Internal Audit function provides independent and objective assurance and the Chief Internal Auditor has an independent reporting line to the Chair of the BAC.

Further information on BRC and BAC is included in the 2021 Accounts.

Figure 2 Board and executive committees

2.10. Risk management

The Society's risk management objectives are to:

1. Identify risks to the Strategic Plan and to the Society's objectives;
2. Assess risk exposures by impact and likelihood; and
3. Respond to risks by evaluating them against the Society's risk appetite, formulating associated management responses and monitoring progress against agreed management action plans.

Risks are identified, assessed, managed, monitored, escalated and reported in accordance with the requirements of the ERMF. Management information captures risk metric information against risk indicators, triggers and limits as appropriate. Where a trigger or limit is breached, an escalation process exists to ensure it is escalated, reported and managed effectively, through the appropriate channels.

2.11. Stress testing and planning

Stress testing, for both internal and external shocks, is used to understand the potential impact of risks crystallising and options to manage them. This includes scenario and contingency planning.

Stress testing is a key part of the Society's capital and liquidity assessments and allows the Board to be satisfied that the Society has sufficient capital and liquidity resources even under a range of severe forward-looking scenarios.

More detail on the stress testing carried out by the Society including the Internal Capital Adequacy Assessment Process (ICAAP) and Internal Liquidity Adequacy Assessment Process (ILAAP) is set out in the sections that follow covering capital, and liquidity and funding risk.

3. Capital resources

3.1. Total available capital and compliance with capital requirements

As at 31 December 2021 and throughout the financial year, the Society complied with the capital requirements in force.

The Society uses the Internal Ratings Based (IRB) approach for most of its retail credit risk and capital management, following approval from the PRA in 2008. For all other lending exposures and for operational risk the Society follows the standardised approach. The standardised approach uses capital risk weighting percentages set by CRD IV[3] to calculate capital requirements.

IRB models are used to calculate capital requirements for prime owner-occupier and buy to let mortgage exposures which account for around 99% of lending exposures throughout 2021 (2020: 99%). The remaining retail credit risk exposures on legacy closed products are modelled using the standardised approach.

Table 4 shows the composition of capital resources for the Society as at 31 December 2021 on a CRD IV basis on both a transitional and end-point basis (i.e. assuming all CRD IV requirements were in force with no transitional provisions permitted).

Transitional provisions apply to the Society's Common Equity Tier 1 (CET 1) capital and CET 1 ratio with a difference between the end-point and transitional disclosures for CET 1 of £2.4 million as at 31 December 2021 (2020: £0.4 million) as a result of amendments to the CRR in response to Covid-19, with the transitional period ending 31 December 2024. Additional Tier 1 (AT 1) and Tier 2 capital (and therefore total capital ratios) include instruments that are grandfathered and are therefore disclosed on both a transitional and end-point basis with the transition period ending on 31 December 2021.

[3] On 28 December 2020 CRD V replaced CRD IV. However, some amendments to related UK regulation will only apply from 31 December 2021.

	Notes	Transitional 2021 £m	Transitional 2020 £m	End-point 2021 £m	End-point 2020 £m
Common Equity Tier 1 (CET 1)					
General reserve		**2,012.6**	1,835.1	**2,012.6**	1,835.1
Fair value through other comprehensive income reserve		**4.5**	2.3	**4.5**	2.3
Cash flow hedge reserve		**27.5**	(46.3)	**27.5**	(46.3)
Common Equity Tier 1 prior to regulatory adjustments		**2,044.6**	1,791.1	**2,044.6**	1,791.1
Common Equity Tier 1 regulatory adjustments					
Prudent additional valuation adjustment[1]	1	**(0.7)**	(1.0)	**(0.7)**	(1.0)
Intangible assets[2]	2	**(32.9)**	(31.0)	**(32.9)**	(31.0)
Cash flow hedge reserve[2]	2	**(27.5)**	46.3	**(27.5)**	46.3
Excess of expected loss over impairment[3]	3	**(31.4)**	(4.0)	**(31.4)**	(4.0)
Pension fund surplus adjustment[2]	2	**(19.9)**	(7.7)	**(19.9)**	(7.7)
Foreseeable distributions[4]	4	**(10.4)**	(10.4)	**(10.4)**	(10.4)
IFRS 9 transitional arrangements	5	**2.4**	0.4	**–**	–
Common Equity Tier 1 capital		**1,924.2**	1,783.7	**1,921.8**	1,783.3
Additional Tier 1 capital (AT 1)					
Permanent Interest Bearing Shares (PIBS)		**16.0**	32.0	**–**	–
Additional Tier 1 - Perpetual Capital Securities (PCS)		**415.0**	415.0	**415.0**	415.0
Total Additional Tier 1 capital		**431.0**	447.0	**415.0**	415.0
Total Tier 1 capital		**2,355.2**	2,230.7	**2,336.8**	2,198.3
Tier 2					
Subordinated debt		**5.5**	11.1	**–**	–
Total Tier 2 capital		**5.5**	11.1	**–**	–
Total capital		**2,360.7**	2,241.8	**2,336.8**	2,198.3
Risk weighted assets					
IRB approach					
Credit risk - retail exposures		**4,265.1**	4,375.7	**4,265.1**	4,375.7
Standardised approach					
Credit risk - retail exposures		**131.2**	138.4	**129.3**	138.1
Credit risk - liquidity book		**91.4**	141.9	**91.4**	141.9
Credit risk - other		**114.9**	102.0	**114.9**	102.0
Credit valuation adjustment risk		**67.1**	47.5	**67.1**	47.5
Operational risk		**635.8**	605.4	**635.8**	605.4
Total risk weighted assets		**5,305.5**	5,410.9	**5,303.6**	5,410.6
Capital ratios (as a percentage of risk weighted assets)	6				
Common Equity Tier 1		**36.3%**	33.0%	**36.2%**	33.0%
Total Tier 1		**44.4%**	41.2%	**44.1%**	40.6%
Total capital		**44.5%**	41.4%	**44.1%**	40.6%

Table 4 CRD IV – transitional and end-point analysis

Notes
1. A prudent valuation adjustment is applied in respect of assets and liabilities held at fair value.
2. Items do not form part of regulatory capital, net of associated deferred tax.
3. The expected loss over accounting provisions is deducted, gross of tax.
4. Foreseeable distributions in respect of AT 1 securities are deducted, net of tax. A prudent valuation adjustment is applied in respect of assets and liabilities held at fair value.
5. Following the implementation of IFRS 9, any increase in impairment provisions may be added back to CET 1 on a reducing basis, over five years. Currently 100% of the increase in provisions is added back to CET 1 as a result of measures bought in as a result of Covid-19.
6. CRD IV sets a minimum for Tier 1 capital of 6% of risk weighted assets (RWAs) of which CET 1 is required to be a minimum of 4.5% of RWAs. The total of Tier 1 and Tier 2 capital must be a minimum of 8% RWAs.

Appendix 1 sets out this information in the template format published by the EBA in 'Implementing Technical Standard (ITS) 2013/01'.

At 31 December 2021, and throughout the year, the Society complied in full with the capital requirements that were in force. The CET 1 ratio increased to 36.2% (2020: 33.0%). Total risk weighted assets decreased by 2.0%. Most of this reduction relates to mortgage risk weighted assets, where the impact of 7.2% growth in the mortgage book has been more than offset by the effects of improved credit conditions and the decrease in LTV discussed in the credit risk section.

The Individual consolidated CET 1 ratio on an end-point basis at 31 December 2021 was 0.8% (2020: 0.7%) higher than the Group ratio due to assets held by entities that sit outside of the individual consolidation.

Table 5 shows the movement in capital during 2021. CET 1 capital is the same on an end-point and transitional basis. Additional Tier 1 (AT 1) and Tier 2 capital (and therefore total capital) are disclosed on a transitional basis.

	Transitional £m
Common Equity Tier 1 capital at 1 January 2021	1,783.7
Retained profit for the year	190.8
Other changes to General reserves	(13.3)
Change in prudent valuation adjustments	0.3
Change in intangible assets	(1.9)
Change in Fair value through other comprehensive income reserve	2.2
Change in expected loss over impairment	(27.4)
Change in pension fund surplus adjustment	(12.2)
Change in IFRS 9 transitional arrangements	2.1
Common Equity Tier 1 capital at 31 December 2021	**1,924.3**
Additional Tier 1 capital at 1 January 2021	447.0
Repurchase / Issuance of AT 1 capital	
Amortisation of PIBS	(16.0)
Additional Tier 1 capital at 31 December 2021	**431.0**
Total Tier 1 capital at 31 December 2021	**2,355.3**
Tier 2 capital at 1 January 2021	11.1
Amortisation of subordinated debt	(5.6)
Tier 2 capital at 31 December 2021	**5.5**
Total regulatory capital at 31 December 2021	**2,360.8**

Table 5 Regulatory capital flow statement

3.2. Tier 1 capital

Tier 1 capital comprises:

- General reserve;
- Fair value through other comprehensive income reserve;
- AT 1 capital – Perpetual Capital Securities (PCS);
- AT 1 capital – Permanent Interest Bearing Shares (PIBS) on a transitional basis only; and
- Adjustments as set out by the regulatory requirements governing capital resources – see Table 4.

The General reserve represents the Society's accumulated accounting profits.

In April 2019, the Society issued £415.0 million of PCS capital. These PCS pay a fully discretionary, non-cumulative fixed coupon at an initial rate of 6.875% per annum with an optional redemption in September 2024. The PCS are convertible into Core Capital Deferred Shares (the equivalent of common shares for a building society) if the Society's CET 1 capital ratio should fall below 7%. The combined cost of the tender and new issuance fees has been recognised within the Society's General reserves.

More information on the key features of these securities is included in Appendix 2.

3.3. Tier 2 capital

Tier 2 capital comprises Subordinated debt (transitional basis only).

Subordinated debt instruments are unsecured and rank behind the claims of all depositors, creditors and shareholders in the Society other than holders of PIBS and PCS.

Appendix 2 shows the key features of the Society's Tier 1 and Tier 2 capital instruments and more information can be found in the 2021 Accounts.

3.4. Leverage ratio

The recent update to the UK leverage ratio framework came into force on 1 January 2022, after the Society's reporting date of 31 December 2021. The framework remains applicable to banks and building societies with retail deposits of above £50 billion and now also covers firms with non-UK assets of £10bn or more. The Society is not currently captured by either of these thresholds. The Society is more likely to exceed the retail deposits threshold in the future, which is not expected in the next three years. If it does exceed the threshold and leverage were to become a capital requirement, our focus on low risk assets means that the leverage requirement will be more onerous and likely become the binding capital requirement on the Society.

The UK leverage ratio requires a minimum ratio of 3.25% calculated on the basis that exposures exclude central bank exposures with less than a 3 month maturity. Of the UK leverage requirement, a maximum of 25% may be met using high quality AT 1 capital. Neither of these modifications exists in the CRR leverage measure where the minimum 3% requirement can be met by Tier 1 capital (CET 1 and AT 1) without restriction.

There are two additional buffers. These are a Supplementary Leverage Ratio Buffer (SLRB), which does not impact the Society, and a macro-prudential Countercyclical Leverage Buffer (CCLB). The levels of these buffers are set at 35% of the corresponding CET 1 buffers – see section 4.4.

The CCLB has, in line with the countercyclical capital buffer rate (CCyB), been at 0% since March 2020, resulting in a minimum UK Leverage of 3.25%. The FPC has confirmed that is increasing the UK CCyB from 0% to 1%, coming into effect from December 2022, which will result in the CCLB increasing to 3.65%.

The Society's Strategic Plan ensures that it will continue to meet the UK leverage requirements on an ongoing basis.

The Society has policies and procedures in place to manage the risk of excessive leverage through maintaining a prudent balance between the pace of growth and the pace of capital accumulation. This includes consideration through the ICAAP of the impact of stress events on leverage. This is explicitly incorporated into the Society's strategic planning process (see section 4.2.2). ICAAP stress testing considers the impact of stress events on leverage.

The Society's leverage ratio position on an end-point basis is set out below on both a UK and CRR basis.

The UK leverage ratio increased to 4.8% (2020: 4.6%). The increase in the UK leverage ratio was the result of eligible Tier 1 capital increasing at a faster rate than leverage ratio exposures excluding central bank exposures with less than a 3 month maturity. This reflects the Society's strategy to remain low risk whilst retaining only sufficient profits to support leverage ratio at required levels. The CRR ratio remained unchanged at 4.3%.

	Notes	**End-point 2021 £m**	End-point 2020 £m
Total Tier 1 capital – used in CRR calculation		**2,336.8**	2,198.3
Adjustment for AT 1 restriction		**(21.1)**	(37.3)
Total Tier 1 capital – used in UK calculation		**2,315.7**	2,161.0
Leverage ratio exposures			
Total balance sheet assets		**54,529.7**	51,498.3
Mortgage pipeline	1	**415.9**	500.8
Other committed facilities (undrawn lending)	1	**13.1**	14.9
Repurchase agreements	2	**74.5**	76.1
Netted derivative adjustments	3	**(141.5)**	27.8
Other adjustments	4	**(92.4)**	(429.7)
Total leverage ratio exposures – used in CRR calculation		**54,799.3**	51,688.2
Adjustment to exclude central bank reserves		**(6,327.7)**	(5,208.2)
Total leverage ratio exposures – used in UK calculation		**48,471.6**	46,480.0
CRR leverage ratio		**4.3%**	4.3%
UK leverage ratio		**4.8%**	4.6%

Table 6 Leverage ratio

Notes

1. Mortgage pipeline are assessed at 20% and other commitments at 50%.
2. Repurchase agreements represent the extent to which collateral provided on repurchase agreements exceeds the amount borrowed.
3. The netted derivative adjustment figure converts the accounting value of derivatives to an exposure measure.
4. Other adjustments predominantly relate to asset balances that have already been included in the capital calculation and these are therefore removed from the total Balance Sheet assets figure.

The CRR leverage ratio disclosures using the European Banking Authority Templates are in Appendix 4.

4. Capital requirements

4.1. Pillar 1

4.1.1. Introduction

The primary purpose of capital is to absorb any losses that might arise. For the Society, capital is principally held for credit losses on lending, trading losses due to pressure on net interest income or expenses and losses from other adverse events such as operational incidents.

The Society manages its capital structure to ensure it continues to hold sufficient capital to meet its business objectives, regulatory requirements and the expectations of other key stakeholders.

The Society employs a number of tools to support the management of capital. The Board is responsible for setting risk appetite with respect to capital and defines minimum levels of capital, primarily by reference to capital ratios, leverage ratios and surplus over regulatory capital requirements. These minimum levels are translated into specific risk metrics which are monitored by the BRC, ERC and the Asset and Liability Committee (ALCO). Day to day capital management is delegated to the Chief Financial Officer (CFO) and Treasurer and overseen by the Risk Function, ALCO, BRC and ultimately the Board.

The Society assesses its capital position and risks through an annual ICAAP. The ICAAP considers the key capital risks and the amount of capital the Society should retain to cover these risks. These requirements are assessed against the current position and throughout the five year Strategic Plan. Regular stress testing is undertaken to enhance the understanding of any potential vulnerabilities to stressed market conditions or tail-risks and management actions that could be deployed to manage these. The ICAAP and stress testing are considered further in section 4.2 below.

4.1.2. Minimum capital requirement – Pillar 1

The Society's minimum capital requirement under Pillar 1 is the sum of the credit risk capital requirement and the operational risk capital requirement. Market risk arises from foreign exchange risk and is calculated in accordance with the Standardised Approach but is set at zero as it falls below the threshold for recognition. The Society does not have a trading book and foreign exchange risk is negligible.

The credit risk capital requirement is largely dependent upon residential mortgage capital calculated under the IRB approach. The remaining credit risk capital requirement is calculated using the Standardised approach. The capital requirement under both the IRB and Standardised approach is calculated as 8% of the risk weighted exposure amounts for each credit risk exposure class.

The operational risk capital requirement is calculated using the Standardised approach based on total income averaged over three years.

The following table shows the Society's assessment of its overall minimum capital requirement.

	RWA		Minimum capital requirements	
	2021 £m	2020 £m	**2021 £m**	2020 £m
Credit risk (excluding counterparty credit risk (CCR))	**4,567.4**	4,722.9	**365.4**	377.8
Of which standardised approach	**302.3**	347.2	**24.2**	27.7
Of which the advanced IRB approach	**4,265.1**	4,375.7	**341.2**	350.1
Counterparty credit risk (CCR)	**91.1**	69.4	**7.3**	5.6
Of which mark to market	**3.6**	2.5	**0.3**	0.2
Of which the standardised approach	**20.4**	19.4	**1.6**	1.6
Of which credit valuation adjustment	**67.1**	47.5	**5.4**	3.8
Securitisation exposures	**2.7**	3.3	**0.2**	0.3
Of which standardised approach (SA)	**2.7**	3.3	**0.2**	0.3
Operational risk	**635.8**	605.4	**50.9**	48.4
Of which standardised approach	**635.8**	605.4	**50.9**	48.4
Amounts below the threshold for deduction (subject to 250%) risk weight	**8.6**	9.9	**0.7**	0.8
Total	**5,305.6**	5,410.9	**424.5**	432.9

Table 7 Minimum capital requirement – Pillar 1

4.1.3. Minimum capital requirement – credit risk

The following table shows the composition of the minimum capital required for credit risk (excluding credit valuation adjustment included in counterparty credit risk in Table 7) at 31 December 2021.

	Notes	2021 £m	2020 £m
Internal Ratings Based (IRB)			
Retail mortgages (prime secured against residential property)		**341.2**	350.1
Standardised exposure classes			
Mortgages and loans		**10.5**	11.1
Of which:			
Retail mortgages secured against residential property		**8.3**	9.5
Corporates (commercial lending)		**0.1**	0.1
Other retail (unsecured loans)		**0.8**	1.0
Past due		**1.3**	0.5
Treasury		**7.3**	11.3
Of which:			
Institutions	1	**7.1**	11.1
Securitisation positions		**0.2**	0.2
Other		**9.2**	8.2
Of which:			
Non-credit obligation assets (fixed assets and other)		**8.5**	7.4
Amounts below the threshold for deduction		**0.7**	0.8
Total minimum capital requirement Standardised		**27.0**	30.6
Total minimum capital requirement IRB and Standardised		**368.2**	380.7

Table 8 Minimum capital requirement for credit risk

Notes
1. Institutions includes minimum capital requirement of £1.3 million for covered bonds (2020: £1.5 million), £0.3 million for central clearing counterparties (2020: £0.2 million) and £0.4 million for equity (2020: £0.4 million).

4.1.4. Movement in credit risk – Risk Weighted Assets (RWAs)

The following table shows the movement in credit risk RWAs (excluding credit valuation adjustment) over 2021.

	IRB mortgages		Standardised mortgages and loans		Treasury		Other		Total	
	RWA amount £m	Capital r'ment £m	RWA amount £m	Capital r'ment £m	RWA amount £m	Capital r'ment £m	RWA amount £m	Capital r'ment £m	RWA amount £m	Capital r'ment £m
RWAs at 1 January 2021	4,375.7	350.1	138.4	11.1	141.9	11.3	102.0	8.2	4,758.0	380.7
Book size increase/(decrease)	861.6	68.9	(23.3)	(1.9)	(50.9)	(4.1)	12.9	1.0	800.3	63.9
Book quality (improvement)/ deterioration	(972.2)	(77.8)	16.1	1.3	0.4	–	–	–	(955.7)	(76.5)
RWAs at 31 December 2021	**4,265.1**	**341.2**	**131.2**	**10.5**	**91.4**	**7.2**	**114.9**	**9.2**	**4,602.6**	**368.1**

Table 9 Risk Weighted Assets (RWA) flow statement

The increase in IRB RWAs attributable to book size is driven by growth of the Society's mortgage book. All new lending is on an IRB basis. Book quality improvements reflect an increase in house prices and lower arrears.

The majority of the treasury book is made up of exposures to central banks and sovereigns, which are zero risk weighted. The book quality improvement relates to movement in exposures to financial institutions subject to lower risk weightings and lower exposure to currency swaps.

The LGD models used for mortgages were submitted to the PRA in Q3 2021 and are awaiting approval. The hybrid PD model recalibration is planned for 2022 and we expect to submit it to the PRA early in H2 2022. We estimate that the new models will have a material impact on risk weights and therefore on the Society's CET 1 ratio.

As an interim measure, from 1 January 2022, the Society has agreed to hold additional RWAs, with initial assessments leading to an increase of 43%, leading to a reduction in the CET 1 ratio for the Society to 26.4%.

4.2. Pillar 2

4.2.1. Introduction

The Pillar 2 capital requirement is firm-specific and set by the PRA to capture risks that are not fully captured by Pillar 1 (see section 4.3 Pillar 2A) and risks to which a firm may become exposed under a severe but plausible stress (Pillar 2B) that are not captured by other buffers. The Society completes an annual assessment of all of its risks and submits this assessment to the PRA to calibrate the Pillar 2 requirements.

4.2.2. Internal Capital Adequacy Assessment Process (ICAAP) and stress testing

The Board determines if the Society has sufficient capital to support the Society's business objectives by undertaking an annual ICAAP in line with the PRA requirements. The ICAAP considers the key capital risks and the amount of capital the Society should retain to cover these risks. These requirements are assessed against the current position and throughout the five year Strategic Plan. The ICAAP includes consideration of Pillar 1 and Pillar 2 requirements.

The calculation of the Pillar 2 requirement examines the Society's business plans in detail, subjecting them to economic and operational stresses over a five year planning horizon. This stress testing, a major part of the ICAAP, assesses whether capital requirements would be met under severe but plausible stress scenarios specified by the regulator. The ICAAP considers what management actions are available to mitigate the impacts of a stress. In 2021, these stresses included a high and low Bank of England Base Rate scenario, and

incorporated further negative trading assumptions to simulate a comprehensive stress on the Society's business model.

The ICAAP also incorporates alternative, more targeted, stress scenarios as part of the overall assessment of capital adequacy risks, including climate change-driven scenarios. Reverse stress testing is also performed to identify very extreme events that have the capacity to 'break' the Society to identify risks and control mechanisms which might otherwise be missed.

This stress testing enables the Society to estimate the magnitude of losses that may be incurred, determine the impact of these losses on the stock of capital available to the Society, and compare this with the additional capital requirements that may be needed in a stressed environment.

Although the stress tests indicate that the Society remains above regulatory minima, potential management actions that could be deployed in a capital stress are considered including the ability to control the rate of asset growth, a cost reduction exercise and the changing of margins on the mortgage and savings portfolios.

Capital levels for the Society are reported to, and monitored by the Board regularly. The Society continues to have a robust level of capital and maintains capital substantially above current regulatory requirements. The Society has a strong Common Equity Tier 1 ratio and the Society's level of regulatory capital surplus will tend to be driven by regulatory changes to calculations of risk weighted assets for mortgages, including changes due to the updates to supervisory statement 11/13 or Basel III reforms and non-risk based measures such as the leverage ratio.

4.3. Pillar 2A

In assessing capital adequacy the Society reviews each of the material inherent risks within its business model. It also reviews the capital needed to support planned growth in lending and operations.

The Society is currently only formally bound by its Total Capital Requirement (TCR) which is set by the PRA. The TCR was last set in 2020 and equates to 10.7% of risk weighted assets or £565.2 million based on year end RWAs (2020: 10.6%, £573.5 million respectively). This includes the Pillar 2A fixed requirement of £141.0 million. The Society comfortably meets this requirement out of its CET 1 capital resources. However, in anticipation of them becoming binding, the Society monitors and seeks to maintain capital sufficient to meet both the non-risk based leverage ratio (under the UK leverage definition) and standardised risk weighted floors that are part of the Basel IV reforms package.

The Society expects the Pillar 2A to be updated to a percentage of risk weighted assets in 2022 as outlined in the recent PRA statement on returning to setting Pillar 2A requirements as a Risk Weighted Asset percentage.

The PRA Pillar 2A risk factors include those not fully covered by Pillar 1 such as credit concentration and operational risks and those risks outside the scope of Pillar 1 such as pension and interest rate risk.

4.4. Regulatory capital buffers

CRD IV requires lenders, to hold supplementary capital buffers. These comprise a Capital Conservation Buffer (CCoB), a Systemic Risk Buffer (SRB), and a macro-prudential Countercyclical Buffer (CCyB). At 31 December 2021, the CCoB was set at 2.5% and the CCyB was 0%. The FPC has confirmed that is increasing the CCyB from 0% to 1%, coming into effect from December 2022. The SRB does not impact the Society as it has total assets of less than £175 billion.

Appendix 5 discloses information relevant for the calculation of the CCyB as at 31 December 2021 in accordance with Regulation (EU) 2015/1555.

4.5. Minimum Requirement for own funds and Eligible Liabilities (MREL)

Minimum Requirement for own funds and Eligible Liabilities (MREL) requirements were introduced by regulators to ensure that taxpayers no longer absorb losses when a bank or building society fails. MREL requirements are set to reflect how complex or important to the wider economy an institution is.

The Society has met an MREL requirement of 18% of RWAs. From 1 January 2023 this will increase to twice the binding capital requirement (or two times Pillar 1 plus Pillar 2A). This currently this equates to 21.3% of RWAs. The Society anticipates the amount of this requirement will increase following upcoming changes to its IRB models and also with the introduction of the Basel IV floors.

Following both the PRA's Policy Statement on the UK Leverage Framework and the Bank of England Policy Statement on MREL, the Society is unlikely to be bound by leverage in the short term. If the UK leverage requirement becomes binding, the level of MREL required would increase substantially and the Society will need to issue MREL eligible debt. The Society's financial plan provides for these outcomes.

4.6. Future regulatory developments

4.6.1. Regulatory Initiatives Grid

An updated version of the Regulatory Initiatives Grid was published in November 2021 by the Financial Services regulators. Key changes from the May 2021 version include:

- Engagement planned for net zero transition in the first half of 2022;
- The publication of a discussion paper on the oversight of critical third parties in 2022;
- The implementation of the remaining Basel III banking standards, which has its key milestone for implementation as post 2023; and
- Consultation on the capital treatment of securitisations of non-performing loans.

There are also updates on regulatory activity in relation to diversity, LIBOR transition, Operational Continuity in Resolution (OCIR), MREL, IRB & Credit risk, PRA109, PRA110, mortgage risk-weight floors and leverage ratio reviews.

The European Commission has proposed its long-awaited legislation that will bring Basel 3.1 into force in the EU via CRD6/CRR3. It published an extensive series of amendments to the EU Capital Requirements Regulation, the Capital Requirements Directive and to the Bank Recovery and Resolution Directive. These proposals modify the international Basel 3.1 standards in timing and substance, in order to limit the expected capital impact they will have on EU banks.

The Commission sets the implementation date as 1 January 2025 for most articles of CRR3, 2 years later than the BCBS deadline, which suggests a similar implementation date for the UK and the PRA. The European proposals are of interest, but the UK will not be expected to comply with CRD6/CRR3.

4.6.2. Dear CEO letter: Reliability of regulatory reporting

The PRA published a letter to Chief Executive Officers (CEOs) highlighting its thematic findings on the reliability of regulatory reporting.

Since October 2019 and as part of its ongoing focus in this area, the PRA have asked firms to demonstrate how they deliver regulatory reporting of appropriate quality. The PRA has also commissioned a number of reports from skilled persons under Section 166 of the Financial Services and Markets Act 2000.

In summary, the PRA has found significant deficiencies in a number of firms' processes for delivering reliable regulatory returns, and it was clear that many firms did not apply the same care and diligence in preparing their

regulatory returns compared with the diligence applied to their financial reporting shared with market counterparties.

The PRA sets out a number of its findings, including in relation to:

- Failures in senior accountability and ownership of the reporting process;
- Failures in controls, including gaps in end-to-end processes for regulatory returns such as insufficient controls around models; and
- Unsatisfactory reconciliation disciplines.

Given the importance of robust regulatory returns, the PRA expect all banks, designated investment firms and building societies to consider the findings in the letter and undertake any work they may need to do to remediate applicable issues, in order to improve their governance, controls, and data related to regulatory reporting. The Society has instigated a programme of improvement work to ensure that requirements in this area continue to be met.

5. Credit risk

5.1. Introduction

Credit risk is the risk that customers or counterparties will not be able to meet their financial obligations to the Society as they fall due. Credit risk is sub-divided into:

- Credit risk for retail exposures (covered in section 5.3); and
- Credit risk for the treasury liquidity book and derivatives (covered in section 5.4).

5.2. Credit risk exposures

The exposures presented below relate to on-balance sheet exposures only. Exposures are presented net of impairment provisions. The limited number of classes disclosed illustrates the Society's very simple business model. All retail credit risk exposures are in the United Kingdom. A distribution of this lending by region is provided in Table 19 Geographical distribution of residential mortgages.

	Notes	**Average during 2021 £m**	**As at 31 December 2021 £m**	Average during 2020 £m	As at 31 December 2020 £m
Residential mortgages	1	**44,987.9**	**46,582.4**	42,764.5	43,393.3
Unsecured and other lending	1	**16.2**	**14.7**	19.5	17.7
Total retail credit risk exposures		**45,004.1**	**46,597.1**	42,784.0	43,411.0
Treasury:					
Central banks and sovereigns	1,2	**6,417.2**	**6,855.1**	5,857.7	5,979.2
Multilateral development banks (supranational bonds)	2	**162.3**	**157.1**	166.5	167.5
Financial institutions	1,2	**865.9**	**589.4**	1,037.6	1,142.4
Residential Mortgage Backed Securities (RMBS)	1,2	**22.9**	**20.4**	22.8	25.4
Total treasury credit risk exposures		**7,468.3**	**7,622.0**	7,084.6	7,314.5
Total credit risk exposures		**52,472.4**	**54,219.1**	49,868.6	50,725.5

Table 10 Credit risk exposure

The international distribution of lending is shown below:

As at 31 December 2021	Notes	**United Kingdom £m**	**Rest of Europe £m**	**Rest of the World £m**	**Total £m**
Residential mortgages	1	**46,582.4**	**–**	**–**	**46,582.4**
Unsecured and other lending	1	**14.7**	**–**	**–**	**14.7**
Total retail credit risk exposures		**46,597.1**	**–**	**–**	**46,597.1**
Treasury:					
Central banks and sovereigns	1,2	**6,855.1**	**–**	**–**	**6,855.1**
Multilateral development banks (supranational bonds)	2	**–**	**106.9**	**50.2**	**157.1**
Financial institutions	1,2	**478.2**	**111.2**	**–**	**589.4**
Residential Mortgage Backed Securities (RMBS)	1	**20.4**	**–**	**–**	**20.4**
Total treasury credit risk exposures		**7,353.7**	**218.1**	**50.2**	**7,622.0**
Total credit risk exposures		**53,950.8**	**218.1**	**50.2**	**54,219.1**

Table 11 Geographical distribution of credit risk 2021

Notes
1. Held at amortised cost using the effective interest method and after deduction of impairment provisions where appropriate.
2. Held at fair value.

As at 31 December 2020	Notes	United Kingdom £m	Rest of Europe £m	Rest of the World £m	Total £m
Residential mortgages	1	43,393.3	–	–	43,393.3
Unsecured and other lending	1	17.7	–	–	17.7
Total retail credit risk exposures		43,411.0	–	–	43,411.0
Treasury:		5,979.2	–	–	5,979.2
Central banks and sovereigns					
Multilateral development banks (supranational bonds)	1,2	–	117.4	50.1	167.5
Financial institutions	1,2	1,024.0	108.5	9.9	1,142.4
Residential Mortgage Backed Securities (RMBS)	2	25.4	–	–	25.4
Total treasury credit risk exposures		7,028.6	225.9	60.0	7,314.5
Total credit risk exposures		50,439.6	225.9	60.0	50,725.5

Table 12 Geographical distribution of credit risk 2020

Notes
1. Held at amortised cost using the effective interest method and after deduction of impairment provisions where appropriate.
2. Held at fair value.

The maturity of exposures is shown on a contractual basis:

As at 31 December 2021	**Notes**	**Up to 12 months £m**	**1-5 years £m**	**5-10 years £m**	**More than 10 years £m**	**Total £m**
Residential mortgages	1	**3,346.7**	**11,836.7**	**12,121.9**	**19,277.1**	**46,582.4**
Unsecured and other lending	1	**1.7**	**4.5**	**5.0**	**3.5**	**14.7**
Total retail credit risk exposures		**3,348.4**	**11,841.2**	**12,126.9**	**19,280.6**	**46,597.1**
Treasury:						
Central banks and sovereigns	1,2	**6,491.8**	**128.6**	**234.7**	**–**	**6,855.1**
Multilateral development banks (supranational bonds)	2	**–**	**157.1**	**–**	**–**	**157.1**
Financial institutions	1,2	**478.7**	**110.7**	**–**	**–**	**589.4**
Residential Mortgage Backed Securities (RMBS)	1	**–**	**13.9**	**–**	**6.5**	**20.4**
Total treasury risk credit exposures		**6,970.5**	**410.3**	**234.7**	**6.5**	**7,622.0**
Total credit risk exposures		**10,318.9**	**12,251.6**	**12,361.5**	**19,287.1**	**54,219.1**

Table 13 Residual maturity of credit risk 2021

As at 31 December 2020	Notes	Up to 12 months £m	1-5 years £m	5-10 years £m	More than 10 years £m	Total £m
Residential mortgages	1	3,167.8	11,124.2	11,406.8	17,694.5	43,393.3
Unsecured and other lending	1	2.0	5.3	5.7	4.7	17.7
Total retail credit risk exposures		3,169.8	11,129.5	11,412.5	17,699.2	43,411.0
Treasury:						
Central banks and sovereigns	1,2	5,510.3	50.2	368.9	49.8	5,979.2
Multilateral development banks (supranational bonds) 2		25.3	142.2	–	–	167.5
Financial institutions	1,2	1,015.5	123.8	3.1	–	1,142.4
Residential Mortgage Backed Securities (RMBS)	1	–	18.2	–	7.2	25.4
Total treasury risk credit exposures		6,551.1	334.4	372.0	57.0	7,314.5
Total credit risk exposures		9,720.9	11,463.9	11,784.5	17,756.2	50,725.5

Table 14 Residual maturity of credit risk 2020

Notes
1. Held at amortised cost using the effective interest method and after deduction of impairment provisions where appropriate.
2. Held at fair value.

5.3. Retail credit risk

5.3.1. Management of retail credit risk

Credit risk in the Society's mortgage book only crystallises in the event that a borrower is unable to repay the mortgage and, as a result, the property on which the mortgage is secured has to be repossessed and sold at a price which is insufficient to allow the borrower to repay the loan.

The Retail Credit Risk Committee (RCRC) and ultimately the Board oversee the Society's credit risk management supported by a specialist retail credit risk department reporting to the CRO.

The Board sets prudent credit risk limits within the context of the Society's overall risk appetite and these are reflected in the Society's lending policy and credit controls. The profile of new lending and performance of the book against these limits is reviewed on a regular basis and reported to RCRC.

All mortgage applications are assessed against the Society's lending policy criteria to ensure consistent credit decision making and lending within the Society's credit risk appetite. This assessment uses stressed interest rates to ensure affordability even if interest rates increase. Assurance that lending decisions are robust and within the Society's policy is provided through the three lines of defence model.

All underwriting is done by the Society and its key lending criteria include:

- Prudent LTV limits;
- A requirement that buy to let loans are against properties which are readily saleable into the owner-occupier market; and
- Restrictions on the maximum number of properties in buy to let portfolios.

The tightening of lending criteria in 2020 to reflect heightened uncertainty about the economy and the housing market as the Covid-19 pandemic evolved has largely been reversed as the economy returns to a more normal footing. Lending policy however is kept under constant review as the effects of new variants of the coronavirus emerge (e.g. Omicron) and the Society is well placed to react quickly if indicators suggest a worsening of economic conditions.

The Society ensures that there is no over-exposure to any geographical region or counterparty and that its mortgage portfolio as a whole can withstand a range of macroeconomic and specific stress scenarios.

5.3.2. The Society's approach to payment difficulties

Inevitably, despite the Society's prudent lending approach, on occasion members experience financial difficulty. This section explains the support the Society has offered to those members and customers in need.

Covid-19 payment holidays

While all Covid-19 related payment holidays have ended during the year the Society has continued to support its customers who have experienced payment difficulties as a result of the Covid-19 pandemic. In total the Society granted 40,101 mortgage payment holidays all of which had expired at 31 December 2021 (2020: active 2,565).

Of the accounts which took a payment holiday, 98.3% had commenced repayments at 31 December 2021 (2020: 98.3%). A further 1.7% had not resumed payments (2020: 1.7%); these accounts had balances of £95.6 million and a balance weighted LTV of 52.0% (2020: £87.6 million, 56.4%). The Society is working with these customers to assess their future affordability. In these cases, the Society seeks to reach a sustainable and fair arrangement to regularise the position in a timeframe which is acceptable to both the Society and the borrower.

Overall arrears have been broadly stable since the start of the pandemic with reductions for customers who have not needed to take a payment holiday and while there are arrears on customers that have taken a payment

holiday, the arrears levels on the main cohorts of payment holidays are stable when compared to arrears levels on these cohorts before they took a payment holiday.

To date we have seen no signs of increased arrears following the end of the furlough scheme at the end of September 2021, and our Collections team have received little contact from customers relating to the end of the furlough scheme.

We are tracking take up of forbearance measures following a Covid-19 payment holiday.

Customers that have taken an extended payment holiday (four to six months) are more likely to be subject to forbearance than customers who have taken a non-extended payment holiday (one to three months), who are in turn more likely to be on forbearance than the remainder of the book.

Arrears performance

During 2021, the Society's longer-term arrears position remained broadly stable at £72.7 million (2020: £72.4 million) of accounts three months or more in arrears. This position has been supported by the government payment holiday and furlough schemes which have ended during the year. Despite this the overall credit quality of the book remains high and arrears levels compare favourably to the UK finance average.

Balances greater than one year in arrears as shown below have continued to increase. This is as a result of the moratorium on house repossessions as part of government Covid-19 measures which ended in mid April 2021. Following this, the Society recommenced activity on previously held possessions and has started moving high arrears cases through litigation, which is anticipated to take longer as court speeds remain impacted as lenders resume activity with demand being higher. Due to the ongoing effects of Covid-19 the Society remains diligent in ensuring it has identified any issues affecting borrowers that may influence our decision to proceed and the Society will only seek repossession of a property when all reasonable efforts have failed or where the mortgage is unsustainable in the longer term. As at 31 December 2021 the Society had 27 properties in possession (2020: 22).

	2021		2020	
	Gross balance £m	**Arrears balance £m**	Gross balance £m	Arrears balance £m
Greater than three months	**68.5**	**2.7**	69.3	2.7
Greater than six months	**34.8**	**2.1**	38.7	2.1
Greater than one year	**15.8**	**1.3**	12.5	1.1
In possession	**4.2**	**0.1**	3.1	0.2

Table 15 Analysis of Society arrears

The accounts in arrears as a percentage of loans and advances to customers reduced during the period with the exception of those cases that are greater than one year in arrears. This is due to the reopening of the economy and for most customers a return to normal payments following payment holidays; however, the ongoing impact of the pandemic for some customers continues. The overall level of arrears remains significantly lower than the UK Finance average, as shown below:

	2021		2020	
	Society %	**UK Finance[1] %**	Society %	UK Finance[1] %
Greater than three months	**0.17**	**0.82**	0.18	0.83
Greater than six months	**0.09**	**0.56**	0.10	0.56
Greater than one year	**0.04**	**0.33**	0.03	0.31
In possession	**0.01**	**0.01**	0.01	0.01

Table 16 Analysis of Society arrears compared with UK Finance

Notes

1. UK Finance data as at 31 December 2021 (31 December 2020).

This trend has been seen in the marginal increase of loans and advances to customers where arrears are more than 2.5% of the balance from 0.09% to 0.10% in 2021 as a result of the increase in possessions following the moratorium; however, this remains far lower than the industry average of 0.67%[1].

Extent and use of forbearance

The Society exercises forbearance if it is in the best interests of the borrower. Forbearance measures that the Society may offer are:

- Concessions, where the Society agrees to accept either the normal monthly payment with no contribution towards paying off the outstanding arrears, reduced payments, or in exceptional circumstances no repayments for a short period;
- Mortgage term extensions to reduce the amount of the monthly payment as part of a longer term solution; and
- A change of product which results in more sustainable monthly payments.

On very rare occasions, arrears may be capitalised or the Society may agree to change repayment mortgages to interest only terms for a temporary period as a means of exercising forbearance.

Where a loan is up to date, the Society may agree a short-term payment holiday as a way of allowing borrowers to resolve financial difficulties, in which case this is treated as a forbearance measure rather than as one where the borrower is using a product feature. Forbearance payment holidays are for a maximum of three months and are only given where the borrower can afford the post-holiday monthly repayments. The table below provides details of loans which have had forbearance measures granted. The Society applies the Prudential Regulation Authority (PRA) definition of forbearance (which aligns to the European Banking Authority) for the purpose of this disclosure and in the period has updated this disclosure to reflect where forbearance measures have been granted in the last 24 months, regardless of whether the incident of forbearance has now been lifted and the loans back on their original terms. This does not include Covid-19 payment holidays which under guidance from the PRA are not considered to be forbearance but does include customers who have previously had Covid-19 payment holidays and then moved onto forbearance measures as a result of entering financial difficulty.

[1] Source: Prudential Regulation Authority - latest available information at 30 September 2021.

	2021		2020	
	No. of accounts	**Carrying value £m**	No. of accounts	Carrying value £m
Forbearance: Accounts past due				
Concessions	**129**	**18.3**	124	15.6
Payment holidays	**45**	**4.5**	46	5.4
Products Transfers	**2**	**0.3**	–	–
Temporary transfer to interest only	**13**	**2.1**	1	0.3
Term extensions	**1**	**0.1**	–	–
Forbearance indicators: Accounts not past due				
Concessions	**189**	**21.4**	198	21.7
Payment holidays	**136**	**15.0**	159	16.4
Products Transfers	**11**	**2.0**	14	2.8
Temporary transfer to interest only	**226**	**52.2**	119	29.1
Term extensions	**2**	**–**	1	0.2
Total Forbearance	**754**	**116.3**	662	91.5
Of which Stage 2	**419**	**70.6**	328	50.5
Of which Stage 3	**247**	**32.8**	209	25.6
ECL on forborne accounts		**0.3**		0.7

Table 17 Forbearance

Notes
1. Prior year information has been updated to reflect forbearance measures granted in the last 24 month to aid comparability, previously disclosed showing measures granted in the last 12 months.
2. In line with guidance from the PRA Covid-19 payment holidays are not considered to be a forbearance measure and are not included within this number.

The number of loans in forbearance has increased compared to 2020 reflecting the impact of the end of government support schemes established to combat Covid-19. This table includes customers who have previously had Covid-19 payment holidays and then moved onto forbearance measures as a result of entering financial difficulty. Despite this increase the average LTV (balance weighted) of accounts in forbearance as at 31 December 2021 remains low at 49.9% (2020: 53.1%) and mitigates the risk of loss to the Society in the event that the borrower defaults on the loan at a future date.

All accounts subject to non-Covid related forbearance are assessed as either stage 2 or 3 under IFRS 9 and the Society recognises a lifetime ECL for these as an impairment provision. Accounts which have had a Covid-19 payment holiday for longer than three months or had a Covid-19 payment holiday of any length and are also showing other signs of credit deterioration are assessed as stage 2 under IFRS 9 where the requirements under the cure period have not yet been met. More information on ECLs is included below.

5.3.3. Retail credit risk profile

The Society continues to focus on low risk, high quality owner-occupier and buy to let mortgages. Non-traditional mortgage lending outside these core segments was discontinued in 2008 and balances on these legacy products, including those acquired as a result of the merger with Stroud & Swindon Building Society in 2010, continue to fall, comprising just 0.3% (2020: 0.4%) of total gross balances at 31 December 2021.

Buy to let lending continues to be provided mainly on an interest only basis reflecting the underlying investment nature of buy to let properties which can be sold to repay the capital amount. Interest only lending was 4.9% of the owner-occupier portfolio at 31 December 2021 (2020: 4.9%) with an average LTV of 34.1% (2020: 37.6%).

Through the early part of 2021 we continued to support customers potentially impacted by the pandemic, in line with government guidance. During 2021 the performance of the mortgage portfolio has been stable with no sign of deterioration including from those customers who took Covid-19 payment holidays.

A summary of the Society's loans and advances to customers by product type is shown below:

Loans and advances to customers	2021 £m	2021 %	2020 £m	2020 %
Residential mortgages: owner-occupier	**27,203.0**	**58.3**	25,508.7	58.7
Residential mortgages: buy to let	**19,237.7**	**41.3**	17,740.7	40.8
Total traditional residential mortgages	**46,440.7**	**99.6**	43,249.4	99.5
Residential near-prime mortgages	**46.7**	**0.1**	53.8	0.1
Residential self-certification mortgages	**112.8**	**0.2**	136.9	0.3
Commercial mortgages[1]	**1.3**	**–**	1.8	–
Total non-traditional mortgages	**160.8**	**0.3**	192.5	0.4
Unsecured personal loans[1]	**14.5**	**–**	17.2	–
Total gross balance	**46,616.0**	**99.9**	43,459.1	99.9
Impairment	**(18.9)**	**–**	(48.1)	(0.1)
Total balance net of impairment	**46,597.1**	**99.9**	43,411.0	99.8
EIR asset, fair value and other adjustments[2]	**23.5**	**0.1**	71.8	0.2
Total net balance	**46,620.6**	**100.0**	43,482.8	100.0

Table 18 Credit risk profile

Notes
1. Legacy books of unsecured personal loans and commercial mortgages.
2. The Effective Interest Rate (EIR) asset and fair value and other adjustments have been presented separately from gross balances in order to aid understanding.

Geographical concentration

The mortgage portfolio is well diversified and reflects the national coverage of the Society's distribution channels. The geographical split of mortgages is shown below and has remained broadly stable:

Region	2021 %	2020 %
London	**27.8**	27.9
South East England	**18.5**	18.7
Central England	**14.0**	14.1
Northern England	**13.2**	13.1
East of England	**11.8**	11.7
South West England	**8.8**	8.8
Scotland	**3.4**	3.4
Wales and Northern Ireland	**2.5**	2.3
Total	**100.0**	100.0

Table 19 Geographical distribution of residential mortgages

Loan to value and income multiples

The low LTV profile of the mortgage book, as shown in the following tables, is a reflection of the Society's low risk approach to lending. The Society updates the estimated value of the properties securing the mortgage portfolio on a quarterly basis using Nationwide regional house price indices and all tables within this report are prepared using these valuations.

The standard maximum income multiple for owner-occupier mortgages is 4.49, a slight reduction on the 4.50 of the prior year. The Society lends on multiples of up to 5.0 for very low LTV cases. Any lending at or above 4.49 times income is closely monitored and by value, 12.6% (2020: 7.8%) of advances were made at or above this level in 2021, which is below the maximum limit of 15% set by the Bank of England's Financial Policy Committee (FPC). The Society reduces maximum income multiples permitted if the loan term extends significantly into retirement to ensure it remains affordable.

The Society is a responsible lender and operates robust affordability checks before advancing any loans. For owner-occupier mortgages, ensuring a borrower has sufficient net income, both at the time of application and in a

future higher interest rate environment, is a key part of this. For buy to let loans the Society sets minimum interest coverage ratios which reflect, among other things, the tax status of borrowers.

The Society's actual average interest coverage ratio at the end of the year using a stressed 5% interest rate was 174.9% (2020: 175.4%), significantly above its minimum lending criteria. The Society also lends to portfolio landlords within the buy to let segment and takes a prudent approach to assessing portfolio LTV and income coverage ratios. There are also limits on the number of properties in the portfolio both in total and those which the Society will lend on. Each loan in a portfolio is assessed on a standalone basis and no allowance is made in the affordability assessment for other income of the borrower.

The LTV distribution of the mortgage book as at 31 December 2021 has improved compared with 2020 as a result of continued growth in House Price Index (HPI) offset by an increase in the 85% to 95% banding as a result of additional lending in the year particularly for first time buyers. The overall average LTV (balance weighted) decreased from 52.8% to 50.9% during the year.

Total mortgage book profile	**2021 %**	2020 %
Indexed loan to value:		
< 50%	**56.7**	53.4
50% to 65%	**27.7**	26.4
65% to 75%	**11.0**	13.6
75% to 85%	**3.1**	5.8
85% to 95%	**1.5**	0.8
> 95%	**–**	–
Total	**100.0**	100.0
Average indexed loan to value of stock (balance weighted)	**50.9**	52.8

Table 20 Total mortgage book loan to value (number of accounts)

The average indexed LTV of loan stock in London has decreased to 51.0% (2020: 51.7%) as a result of increases in house prices during the year. The rest of the portfolio has also seen indexed LTV fall to 50.7% (2020: 53.3%).

The average LTV of gross new lending in 2021 is shown below. In 2021 owner-occupier lending increased reflecting the active house purchase market during the year, in particular during the stamp duty holiday, with continued strong performance in remortgages both for owner-occupier and buy to let.

The average LTV of the new lending book has marginally increased during the year.

Gross lending	**2021 %**	2020 %
Owner-occupier purchase	**39.5**	34.9
Owner-occupier remortgages	**24.5**	23.1
Owner-occupier further advances	**2.0**	2.1
Buy to let purchase	**12.2**	8.1
Buy to let remortgages	**21.0**	31.1
Buy to let further advances	**0.8**	0.7
Total	**100.0**	100.0
Average loan to value (balance weighted)	**64.8**	63.7

Table 21 Gross lending new business profile

5.3.4. IRB rating system

The Society uses IRB models to calculate capital requirements for prime owner-occupier and buy to let mortgage exposures which account for over 99% of lending exposures throughout 2021 (2020: 99%). The remaining retail credit risk exposures on legacy closed products are modelled using the standardised approach.

The models that were in use at 31 December 2021 were approved by the PRA for use in 2020. During 2021 a new suite of models was developed to meet the expectations in the updated version of supervisory statement 11/13 that comes into force on 1 January 2022. These new models were developed on a Definition of Default that meets the applicable guidance (90 Days Past Due trigger, with Unlikeliness to Pay Indicators and incorporating a suitable "cure" period), and consist of:

- LGD models – including new requirements to model Loss Given Cure as well as Loss Given Default, within the parameters of a defined downturn (we used the 2007/08 Credit Crisis);
- EAD model – updated to reflect the defined Credit Crisis downturn; and
- Hybrid PD model – the 2020 model was already built on a hybrid basis but further work was required to assess the level of cyclicality of the PD model, which will result in a model recalibration (increase in PD) in 2022.

The models have significant margins of conservatism incorporated within their calibrations.

The LGD models were submitted to the PRA in Q3 2021 and are awaiting approval. The hybrid PD model recalibration is planned for 2022 and we expect to submit it to the PRA early in H2 2022. We estimate that the new models will have a material impact on risk weights and therefore on the Society's CET 1 ratio.

As an interim measure, from 1 January 2022, the Society has agreed to hold additional RWAs, with initial assessments leading to an increase of 43%, leading to a reduction in the CET 1 ratio for the Society to 26.4%.

Capital is calculated using the Standardised approach on certain small legacy portfolios. No new lending has been originated on these products for a number of years (a drawdown facility is available for a small element of existing equity release customers).

The internal rating model and process

Three models provide the rating of credit risk:

- The Probability of Default model;
- The Loss Given Default model; and
- The Exposure at Default model.

Probability of default model

Credit scores are used to allocate exposures to risk grades. There are separate scorecards for the buy to let and owner-occupier portfolios. Once allocated to a risk grade, the probability of default (PD) model provides a "long run" estimate of the PD for the grade. The PD model is a hybrid model which aims to deliver a PD through time that is neither too point-in-time nor too through-the-cycle (the more point-in-time, the more cyclical the model). The PRA's guidance for calibrating the PD has been used.

Following discussion with the PRA the Society is aware that the resultant level of cyclicality in the final model will require moderation and has developed a plan to address this. It expects to submit a recalibrated model with lower cyclicality around the start of H2 2022.The credit scores of new applications generated by the application scorecards are determined using a combination of loan data, borrower credit details, and, in the case of the buy to let model, information about the rental property.

Behavioural scores are calculated using a combination of internal mortgage performance data together with regular updates of the borrower's credit behaviour with other lenders.

Depending on the length of time the account has been on the books, the application credit score, behavioural credit score, or a blend of the two is used to determine the risk grade for the account and therefore the long run PD to be used in the capital calculation.

Loss given default model

The loss given default (LGD) model uses internal data and is calibrated to downturn economic conditions for use in the regulatory capital calculations.

The model assesses the probability of repossession once an account defaults (PPD), the forced sale discount that is likely to be experienced in selling a property from possession (the 'haircut') and, if repossessed, the likelihood and amount of loss.

As described above, the LGD model will be supplemented by a new Loss Given Cure model once PRA approval is gained, that captures the effect of lost income from non-performing accounts that did not go to possession and realised losses.

Exposure at default model

The exposure at default (EAD) model calculates the balance of accounts at the point of default using a combination of estimated time to default and the interest payments that will be missed.

The combination of PD, LGD and EAD models is used to determine the expected loss and capital requirement for all mortgages within the retail IRB exposure class.

Comparison of impairment provisions with regulatory expected losses

The £13.3m million IFRS 9 impairment provision on IRB loans recognised in the financial statements at 31 December 2021 differs from the £43.4 million determined from the IRB regulatory expected loss models due to the methodology differences set out below.

The IFRS 9 / IRB methodology differences are as follows:

- The IFRS 9 PD is an estimate of the residual lifetime probability of default based on expectations for future economic conditions at the balance sheet date. The first 12 months of the residual lifetime PD estimate is utilised for accounts in Stage 1 whilst the full residual lifetime PD is used for accounts in Stages 2 and 3. The regulatory PD is a long run average throughout a full economic cycle;
- The IFRS 9 EAD has been modelled based on expected payments over the term up to the point of default. The regulatory EAD cannot be lower than the current balance;
- The IFRS 9 LGD includes the impact of future economic conditions such as changes in value of collateral and does not include any floors. Only costs associated with obtaining/selling the collateral are included and the discounting of the expected cash flows is performed using the effective interest rate of the loan. The regulatory LGD is based on downturn conditions and includes all collection costs, is subject to regulatory floors and is discounted using a stressed measure of the cost of capital; and
- IFRS 9 also requires the use of multiple economic scenarios to calculate a probability weighted forward looking ECL.

Allocation of exposures to risk grades by the IRB rating system

The following table shows the Society's retail exposures under IRB.

PD bands up to and including:	Exposure at default estimate 2021 £m	Average loss given default 2021 %	Average risk weight 2021 %	RWAs 2021 £m	Exposure at default 2020 £m	Average loss given default 2020 %	Average risk weight 2020 %	RWAs 2020 £m
0.10	**6,197.2**	**7.4**	**1.1**	**67.1**	6,014.1	8.2	1.2	73.0
0.20	**21,802.4**	**11.5**	**3.6**	**784.8**	20,409.0	12.8	4.0	818.9
0.30	**11,570.1**	**15.2**	**8.2**	**948.5**	11,103.8	16.6	8.9	987.9
0.50	**5,555.0**	**18.9**	**15.4**	**857.2**	5,293.4	19.7	16.1	849.7
1.00	**84.6**	**6.6**	**7.0**	**5.9**	110.4	7.6	8.2	9.0
3.00	**2,183.6**	**20.4**	**33.7**	**736.6**	2,045.9	20.5	34.0	694.9
9.99	**929.5**	**20.3**	**63.9**	**593.9**	921.5	20.3	64.5	594.5
99.99	**289.1**	**11.3**	**57.4**	**166.1**	291.9	13.8	71.2	207.9
In Default	**165.7**	**7.5**	**79.6**	**131.8**	188.5	8.3	74.2	139.9
Total	**48,777.2**			**4,291.9**	46,378.5			4,375.7

Table 22 Allocation of exposures (including undrawn) to IRB risk band

The PDs disclosed in the table above are on a long run basis. The average loss given default and the average risk weights decreased during 2021 as a result of the improving credit quality of the book and the reduction in average LTV of the mortgage book with HPI increases in the year.

Treatment of undrawn exposures

At any point the Society has a number of undrawn exposures that it assigns ratings to using the IRB rating system. These undrawn exposures relate to mortgage applications that have reached the 'offer' stage, where the Society has agreed to advance the funds, but completion of the mortgage has not yet taken place. An offer will generally only be cancelled if adverse information is received after the offer has been made or if it has not been taken up by the customer and hence expires. To assess credit risk it is assumed that all offers will complete, and therefore a conservative conversion factor of 100% is assigned to these undrawn exposures.

At 31 December 2021, the value of undrawn exposures being rated under the IRB approach was £2,105.7 million (2020: £2,534.0 million).

5.3.5. Controls and governance

The Society has a Board approved policy on model risk which defines the standards to be applied to mitigate the risk. This policy is supported by the Model Risk Framework (MRF). The MRF defines key governance requirements and processes for the critical models and calculators used throughout the Society. The Chief Financial Officer is accountable for managing model risk within the Society with independent oversight being the responsibility of the Chief Risk Officer.

The Society continued to strengthen its management of model risk in 2021 through the Model Risk Committee (MRC) which has the purpose of ensuring the exposure faced by the Society remains within the appetite prescribed by the Board. Two new technical sub-committees of MRC were established to support its work, the Retail Credit Models Committee (RCMC) and Financial Models Committee (FMC). RCMC and FMC discuss detailed credit and financial model developments, model performance monitoring, model validation reports and make recommendations to MRC on model updates and redevelopments. MRC also receives updates on progress against actions raised by internal and external reviews of the models falling within the scope of the MRF, and on an annual basis reviews and approves the MRF itself.

The MRF categorises models and complex calculators dependent on their criticality and complexity and the framework operates to require increased controls on more critical and more complex models.

The MRF prescribes certain requirements for critical models that must be met in order for these models to remain in continued use including compliance with governance and formal approval from the MRC. These include:

- Annual first line reviews of the models and independent oversight of these annual reviews.
- Independent model validation of new and incumbent models, with high criticality models validated on an annual basis.
- Governance around model assumptions, compliance and data including sensitivity analysis.
- Model overview statements which identify conditions when the models may fail.
- Requirements on model development and documentation.

In addition, for regulatory capital models, an annual self-assessment against Capital Requirements Regulations and applicable PRA Supervisory Statements is undertaken in order to attest to their compliance with prevailing regulations.

Model risk outlook

IRB models have been and will continue to be subject to significant regulatory reform with regulations published by UK and global bodies. The Society will continue to update its suite of IRB models to reflect changes in regulatory requirements.

See additional information on Model risk within the Risk Management Report in the 2021 Accounts.

5.3.6. IRB model performance over time

Back testing methodologies are applied to assess model performance. Results from these exercises continue to show that models are conservative against actual outcomes.

For capital calculations, the PD and LGD models are calibrated to long run or downturn conditions respectively. This means that in current economic conditions the outputs of both models are significantly higher than actual outcomes. The models will become increasingly conservative with the introduction of the IRB model changes in 2022.

The IRB models are built on a definition of default that is calibrated to 90 days past due together with expanded unlikeliness-to-pay indicators and with an appropriate cure period.

The PD model has been directly calibrated to a hybrid long run average PD rather than on a point-in-time basis. The assessment of performance that has been made therefore compares actual default rates with the long run PD estimate. For comparison the prior year's performance on the same basis is shown within the table below.

The LGD model has also been built on the same definition of default. The table below compares the predicted LGD of accounts that defaulted in 2020 with the actual loss for those accounts that then went on to sell from possession in 2021. The prior year's performance has also been shown (i.e. defaulted in 2019, sold in 2020). The moratorium on possessions that was in operation for much of 2020 and 2021 because of the Covid pandemic has resulted in very few accounts that defaulted in 2020 and sold in 2021, with only three sales resulting in a loss. On two of the three sales the property was abandoned and in poor condition, which had the effect of magnifying the loss. This makes an assessment of the LGD model's performance very difficult, but the results (which display a model under-prediction) are shown for completeness.

The EAD model has also been built to reflect the definition of default. The ratio of estimated to actual EAD is also shown (a ratio of greater than 1 indicates that estimated EAD was greater than actual EAD). The EAD model slightly over-predicts the actual exposure at default.

IRB retail mortgages	Actual 2021 %	Predicted 2021 %	Updated[1] Actual 2020 %	Updated[1] Predicted 2020 %
PD	**0.21**	**0.68**	0.24	0.74
LGD	**15.5**	**11.6**	17.6	18.9
EAD (Estimated to actual)	**1.00**	**N/A**	1.03	N/A

Table 23 Actual PD, LGD and EAD against predicted

Notes
1. Updated positions for 2020 using the new IRB models to aid comparability.

5.3.7. Credit risk mitigation

The Society does not employ credit risk mitigation techniques in relation to retail credit risk apart from taking a first legal charge on each property being offered as security for a mortgage.

All properties taken as security are valued at the outset of the loan and when any further advance is made during the lifetime of the loan.

The initial valuations of properties are determined by the Credit Risk function using a variety of techniques. These techniques include internal physical inspection with written reports by a qualified Royal Institutions of Chartered Surveyors (RICS) surveyor as well as Automated Valuation Models (AVM) and remote surveys. The Credit Risk function oversees the techniques used, and independently assesses the accuracy of valuations which are performed.

Regular reviews of the appropriateness and accuracy of the various valuation methods used by the Society are undertaken, to ensure these remain appropriate.

Assumptions regarding realisation (or work-out) costs, the time it takes to effect repossession and sale, and the effect of forced sale on estimated property values are updated regularly and are used in the impairment model to determine the realistic value that could be achieved upon repossession and sale of a property. Conservative, stressed values for these assumptions are used in calculating the regulatory capital requirement.

5.3.8. Identifying impaired loans

Under IFRS 9 the Society calculates impairment provisions on loans and advances to customers on an expected credit loss (ECL) basis and not on an incurred loss basis. ECL provisions are based on an assessment of PD, LGD and EAD in a range of forward-looking scenarios.

IFRS 9 requires the Society to categorise customer loans into one of three stages at the balance sheet date. Assets that are ‘performing’ are shown in stage 1; assets where there has been a significant increase in credit risk (SICR) since initial recognition or ‘deteriorating’ assets are in stage 2; and accounts which are credit impaired or in ‘default’ are in stage 3. Under IFRS 9, loans are generally treated as being in ‘default’ if they are three or more months in arrears, have been three or more months in arrears in the last 12 months or have other specific unlikeliness to pay indicators. Equity release loans are treated as being in default once the loan is 12 months past the contractual trigger event. IFRS 9 requires a 12 month ECL provision on all stage 1 assets and a lifetime ECL provision on all stage 2 and 3 assets.

More information on the accounting judgements which have been applied are included in the 2021 Accounts.

At 31 December 2021, 92.7% of the Society’s loans and advances to customers were within the stage 1 ‘performing’ category (2020: 91.3%). This proportion has increased during 2021 as a result of the improved credit environment.

The table below shows gross loans and advances to customers split by IFRS 9 stage at 31 December 2021 and at 31 December 2020. For loans in stages 2 and 3, further analysis of accounts which are past due and not past due is also shown.

2021	**Stage 1 'Performing' £m**	**Stage 2 'Deteriorating' £m**	**Of which: Not past due £m**	**Of which: Past due £m**	**Stage 3 'Default' £m**	**Of which: Not past due £m**	**Of which: Past due £m**	**Total £m**
Residential mortgages:								
Owner-occupier	25,078.1	2,022.3	1,9790.8	51.5	102.6	48.1	60.8	**27,203.0**
Buy to let	18,051.9	1,127.6	1,090.5	37.1	58.2	21.6	36.6	**19,237.7**
Total traditional residential mortgages	**43,130.0**	**3,149.9**	**3,061.3**	**88.6**	**161.0**	**63.4**	**97.4**	**46,440.7**
Non-traditional mortgages:								
Residential near-prime	19.5	14.6	13.6	1.0	12.6	6.3	6.3	**46.7**
Residential self-certified	39.4	58.4	56.1	2.3	15.0	9.3	5.7	**112.8**
Commercial lending	–	1.0	1.0	–	0.3	0.3	–	**1.3**
Total non-traditional mortgages	**58.9**	**74.0**	**70.7**	**3.3**	**27.9**	**15.9**	**12.0**	**160.8**
Unsecured loans	**11.9**	**2.3**	**2.1**	**0.2**	**0.3**	**0.2**	**0.1**	**14.5**
Total gross loans	**43,200.8**	**3,226.2**	**3,134.1**	**92.1**	**189.0**	**79.5**	**109.5**	**46,616.0**
	%	**%**	**%**	**%**	**%**	**%**	**%**	**%**
% Total gross loans	**92.7**	**6.9**	**6.7**	**0.2**	**0.4**	**0.2**	**0.2**	**100.0**

Table 24 Gross loans and advances to customers split by IFRS 9 stage 2021

2020	Stage 1 'Performing' £m	Stage 2 'Deteriorating' £m	Of which: Not past due £m	Of which: Past due £m	Stage 3 'Default' £m	Of which: Not past due £m	Of which: Past due £m	Total £m
Residential mortgages:								
Owner-occupier	23,089.8	2,300.3	2,252.4	47.9	118.6	54.7	63.9	25,508.7
Buy to let	16,532.8	1,152.3	1,122.1	30.2	55.6	21.7	33.9	17,740.7
Total traditional residential mortgages	39,622.6	3,452.6	3,374.5	78.1	174.2	76.4	97.8	43,249.4
Non-traditional mortgages:								
Residential near-prime	21.1	18.7	17.3	1.4	14.0	5.6	8.4	53.8
Residential self-certified	45.6	73.6	72.1	1.5	17.7	8.3	9.4	136.9
Commercial lending	–	1.4	1.4	–	0.4	0.4	–	1.8
Total non-traditional mortgages	66.7	93.7	90.8	2.9	32.1	14.3	17.8	192.5
Unsecured loans	14.1	2.8	2.5	0.3	0.3	0.2	0.1	17.2
Total gross loans	39,703.4	3,549.1	3,467.8	81.3	206.6	90.9	115.7	43,459.1
	%	%	%	%	%	%	%	%
% Total gross loans	91.3	8.2	8.0	0.2	0.5	0.2	0.3	100.0

Table 25 Gross loans and advances to customers split by IFRS 9 stage 2020

At the reporting date, 92.7% of loans are in stage 1 with 6.9% in stage 2 and 0.4% in stage 3 (2020: 91.3%, 8.2% and 0.5%). Cure periods are applied to accounts in stages 2 and 3 which have had a Covid-19 payment holiday in addition to accounts which have hit certain quantitative triggers such as arrears. These cure periods delay transition of loans to a lower credit risk classification (i.e. from stage 3 to stage 2 or from stage 2 to stage 1) by requiring 12 months of sustained performance before a loan is reassessed. As a result, loans can be recorded in stage 2 or stage 3 despite otherwise performing at the reporting date.

Stage 2 balances were £3,226.2 million (2020: £3,549.1 million) and of these £92.1 million or 2.9% (2020: £81.3 million, 2.3%) are in arrears by 30 days or more. A total of £1,930.0 million (2020: £2,604.1 million) are present

within stage 2 as a result of the SICR criteria established in 2020 as a result of the Covid-19 pandemic of which none (2020: £324.9 million or 9.2%) have an active Covid-19 payment holiday at 31 December 2021. All £1,930.0 million of these accounts (2020: £2,561.5 million or 98.4%) were paid up to date as at 31 December 2021 and remain in stage 2 as a result of cure rules or other indicators of increased risk. The reduction in stage 2 balances in the period is predominantly as a result of the cure of these Covid-19 balances transferring back into Stage 1 following application of the cure rules.

Of the £189.0 million (2020: £206.6 million) of loans which are classified as stage 3 at the reporting date, 38.5% or £72.4 million were greater than three months in arrears (2020: 35.0%, £72.4 million), and 42.1% or £79.5 million were paid up to date (2020: 44.0%, £90.9 million). This position has deteriorated slightly in the year as a result of the moratorium on repossessions which, while it has now ended, has led to delays in loans which have defaulted not moving through to possession. At 31 December 2021 the number of properties which were in possession remained low; a total of £4.2 million of stage 3 loans were in possession (2020: £3.1 million), representing 27 individual properties (2020: 22 properties).

The table below shows total impairment provision split by IFRS 9 stage at 31 December 2021 and the previous year. For stages 2 and 3, further analysis of accounts which are past due and not past due is also shown.

			Of which			Of which		
Impairment provision as at 31 December 2021	**Stage 1 12 month ECL £m**	**Stage 2 lifetime ECL £m**	**Not past due £m**	**Past due £m**	**Stage 3 lifetime ECL £m**	**Not past due £m**	**Past due £m**	**Total £m**
Residential mortgages:								
Owner-occupier	**1.2**	**5.0**	**5.0**	**–**	**2.5**	**1.8**	**0.7**	**8.7**
Buy to let	**2.3**	**3.2**	**3.1**	**0.1**	**3.0**	**1.7**	**1.3**	**8.5**
Total traditional residential mortgages	**3.5**	**8.2**	**8.1**	**0.1**	**5.5**	**3.5**	**2.0**	**17.2**
Non-traditional mortgages:								
Residential near-prime	**–**	**–**	**–**	**–**	**0.1**	**0.1**	**–**	**0.1**
Residential self-certified	**–**	**0.1**	**0.1**	**–**	**0.3**	**0.3**	**–**	**0.4**
Commercial lending	**–**	**0.1**	**0.1**	**–**	**0.1**	**0.1**	**–**	**0.2**
Total non-traditional mortgages	**–**	**0.2**	**0.2**	**–**	**0.5**	**0.5**	**–**	**0.7**
Unsecured loans	**0.1**	**0.6**	**0.5**	**0.1**	**0.2**	**0.1**	**0.1**	**0.9**
Mortgage pipeline	**0.1**	**–**	**–**	**–**	**–**	**–**	**–**	**0.1**
Total impairment provision	**3.7**	**9.0**	**8.8**	**0.2**	**6.2**	**4.1**	**2.1**	**18.9**
	%	**%**	**%**	**%**	**%**	**%**	**%**	**%**
Total impairment provision	**19.6**	**47.6**	**46.5**	**1.1**	**32.8**	**21.7**	**11.1**	**100.0**

Table 26 Impairment on loans and advances to customers split by IFRS 9 stage 2021

Impairment provision as at 31 December 2020	Stage 1 12 month ECL £m	Stage 2 lifetime ECL £m	Of which Not past due £m	Of which Past due £m	Stage 3 lifetime ECL £m	Of which Not past due £m	Of which Past due £m	Total £m
Residential mortgages:								
Owner-occupier	4.8	16.5	16.4	0.1	5.2	3.7	1.5	26.5
Buy to let	3.5	10.3	10.2	0.1	4.7	2.7	2.0	18.5
Total traditional residential mortgages	8.3	26.8	26.6	0.2	9.9	6.4	3.5	45.0
Non-traditional mortgages:								
Residential near-prime	0.1	0.2	0.2	–	0.2	0.1	0.1	0.5
Residential self-certified	–	0.5	0.5	–	0.7	0.4	0.3	1.2
Commercial lending	–	0.2	0.2	–	0.2	0.2	–	0.4
Total non-traditional mortgages	0.1	0.9	0.9	–	1.1	0.7	0.4	2.1
Unsecured loans	0.1	0.7	0.6	0.1	0.1	0.1		0.9
Mortgage pipeline	0.1	–	–	–	–	–	–	0.1
Total impairment provision	8.6	28.4	28.1	0.3	11.1	7.2	3.9	48.1
	%	%	%	%	%	%	%	%
Total impairment provision	17.9	59.0	58.4	0.6	23.1	15.0	8.1	100.0

Table 27 Impairment on loans and advances to customers split by IFRS 9 stage 2020

A reconciliation of movements in gross exposures and impairment provision by IFRS 9 stage from 1 January to 31 December 2021 is as follows:

	Stage 1		Stage 2		Stage 3		Total	
	Gross balance £m	Provision 12 month ECL £m	Gross balance £m	Provision 12 month ECL £m	Gross balance £m	Provision 12 month ECL £m	Gross balance £m	Provision £m
At 1 January 2021	**39,703.4**	**8.6**	**3,549.1**	**28.4**	**206.6**	**11.1**	**43,459.1**	**48.1**
Movements with Income Statement impact:								
Transfer from stage 1 to stage 2	(1,160.0)	(0.1)	1,160.0	3.5	–	–	–	3.4
Transfer from stage 1 to stage 3	(27.4)	–	–	–	27.4	0.5	–	0.5
Transfer from stage 2 to stage 3	–	–	(65.9)	(0.3)	65.9	0.3	–	–
Transfer from stage 3 to stage 2	–	–	40.0	0.7	(40.0)	(0.7)	–	–
Transfer from stage 3 to stage 1	14.1	–	–	–	(14.1)	(0.1)	–	(0.1)
Transfer from stage 2 to stage 1	948.4	0.1	(948.4)	(0.6)	–	–	–	(0.5)
Net movement arising from transfer of stages	**(224.9)**	**–**	**185.7**	**3.3**	**39.2**	**–**	**–**	**3.3**
New loans originated[1]	10,452.3	0.8	51.2	–	1.3	–	10,504.8	0.8
Remeasurement of ECL due to changes in risk parameters	–	–	–	(0.9)	–	(1.7)		(2.6)
Increase/(decrease) in post model adjustments	–	(5.3)	–	(21.4)	–	(1.6)		(28.3)
Remeasurement of ECL due to model refinements	–	0.2	–	–	–	–		0.2
Loans derecognised in the period	(4,894.6)	(0.6)	(431.2)	(0.4)	(48.0)	(1.0)	(5,373.8)	(2.0)
Other items impacting income statement charge/(reversal)	–	–	–	–	–	(0.1)	–	(0.1)
Net write offs directly to Income Statement	–	0.1	–	–	–	(0.1)	–	–
Income Statement release for the period		**(4.8)**		**(19.4)**		**(4.5)**		**(28.7)**
Repayment and charges	(1,835.3)	–	(128.6)	–	(9.2)	–	(1,973.1)	–
Net write offs	(0.1)	(0.1)	–	–	(0.9)	(0.4)	(1.0)	(0.5)
At 31 December 2021	**43,200.8**	**3.7**	**3,226.2**	**9.0**	**189.0**	**6.2**	**46,616.0**	**18.9**

Table 28 Reconciliation of movements in gross exposures and impairment provision by IFRS 9 stage 2021

Notes
1. New mortgages originated in stages 2 and 3 relate to further advances on accounts which are performing at the date of origination but are in the 12 month cure period for IFRS 9 staging.

	Stage 1		Stage 2		Stage 3		Total	
	Gross balance 12 month ECL £m	Provision 12 month ECL £m	Gross balance lifetime ECL £m	Provision lifetime ECL £m	Gross balance lifetime ECL £m	Provision lifetime ECL £m	Gross balance £m	Provision £m
At 1 January 2020	40,893.1	1.0	1,078.6	3.2	197.3	7.8	42,169.0	12.0
Movements with Income Statement impact:								
Transfer from stage 1 to stage 2	(3,104.2)	(0.1)	3,104.2	0.5	–	–	–	0.4
Transfer from stage 1 to stage 3	(39.1)	–	–	–	39.1	0.9	–	0.9
Transfer from stage 2 to stage 3	–	–	(57.5)	(0.2)	57.5	0.2	–	–
Transfer from stage 3 to stage 2	–	–	36.9	0.9	(36.9)	(0.9)	–	–
Transfer from stage 3 to stage 1	10.8	0.1	–	–	(10.8)	(0.1)	–	
Transfer from stage 2 to stage 1	303.0	–	(303.0)	(0.4)	–	–	–	(0.4)
Net movement arising from transfer of stages	(2,829.5)	–	2,780.6	0.8	48.9	0.1	–	0.9
New loans originated[1]	6,981.1	0.5	2.5	–	–	–	6,983.6	0.5
Remeasurement of ECL due to changes in risk parameters	–	(4.7)	–	4.5	–	1.7	–	1.5
Increase/(decrease) in post model adjustments	–	12.0	–	19.4	–	2.2	–	33.6
Remeasurement of ECL due to model refinements[2]	–	0.1	–	0.9	–	1.0	–	2.0
Loans derecognised in the period	(3,698.9)	(0.3)	(233.3)	(0.4)	(32.1)	(0.7)	(3,964.3)	(1.4)
Other items impacting income statement charge/(reversal)	–	–	–	–	–	(0.3)	–	(0.3)
Net write offs directly to Income Statement	–	–	–	–	–	(0.4)	–	(0.4)
Income Statement charge for the period		7.6		25.2		3.6		36.4
Repayment and charges	(1,642.4)	–	(79.3)	–	(6.4)	–	(1,728.1)	–
Net write offs	–	–	–	–	(1.1)	(0.3)	(1.1)	(0.3)
At 31 December 2020	39,703.4	8.6	3,549.1	28.4	206.6	11.1	43,459.1	48.1

Table 29 Reconciliation of movements in gross exposures and impairment provision by IFRS 9 stage 2020

Notes

1. New mortgages originated in stages 2 and 3 relate to further advances on accounts which are performing at the date of origination but are in the 12 month cure period for IFRS 9 staging.
2. A number of refinements to the Society's ECL models have been made during 2020. These include an update to the calculation of the Probability of Default and an enhancement to the regional house price index modelling capability. In the year these refinements decreased ECLs by £1.1 million on a group consolidation basis and £0.4 million on an unconsolidated basis.

The Society updates its security values using the Nationwide Building Society quarterly regional HPI. Part of the risk assessment of the portfolio also includes an initial individual revaluation of security using AVM values, and following model build and testing it is expected that the Society will use AVM values more widely in future.

The LTV distribution of the mortgage book by IFRS 9 stage has increased slightly during 2021 with 93% of the mortgage book having an LTV of 75% or lower (2020: 90%). The increase in the higher LTV bandings has been driven by increased lending in this area in the year, in particular to first time buyers. However, the overall average LTV (balance weighted) of the book decreased from 52.8% to 50.9% during the year. This is shown by IFRS 9 stage below:

As at 31 December 2021 **Indexed loan to value**	**Stage 1** **'Performing'** **£m**	**Stage 2** **'Deteriorating'** **£m**	**Stage 3** **'Default'** **£m**	**Impairment** **£m**	**Total** **£m**
< 50%	**19,621.1**	**1,344.1**	**95.1**	**(1.5)**	**21,058.8**
50% to 65%	**14,271.5**	**1,174.6**	**60.9**	**(5.3)**	**15,501.7**
65% to 75%	**6,250.1**	**580.3**	**23.8**	**(4.7)**	**6,849.5**
75% to 85%	**2,080.0**	**112.1**	**5.7**	**(2.2)**	**2,195.6**
85% to 90%	**670.4**	**8.2**	**0.5**	**(0.4)**	**678.7**
90% to 95%	**275.6**	**3.8**	**0.1**	**(0.3)**	**279.2**
95% to 100%	**19.7**	**0.3**	**0.1**	**–**	**20.1**
> 100%	**0.5**	**0.5**	**2.5**	**(1.3)**	**2.2**
Unsecured loans	**11.9**	**2.3**	**0.3**	**(0.9)**	**13.6**
Mortgage pipeline	**–**	**–**	**–**	**(0.1)**	**(0.1)**
Other[1]	**–**	**–**	**–**	**(2.2)**	**(2.2)**
Total	**43,200.8**	**3,226.2**	**189.0**	**(18.9)**	**46,597.1**

Table 30 Loan to value distribution by IFRS 9 stage 2021

Notes
1. Other includes expected credit losses which are not directly attributable to underlying accounts and therefore are not allocated across loan to value bandings.

As at 31 December 2020 Indexed loan to value	Stage 1 'Performing' £m	Stage 2 'Deteriorating' £m	Stage 3 'Default' £m	Impairment £m	Total £m
< 50%	16,802.1	1,187.7	86.8	(1.3)	18,075.3
50% to 65%	12,595.2	1,130.7	62.8	(8.0)	13,780.7
65% to 75%	6,354.8	764.7	32.5	(14.4)	7,137.6
75% to 85%	3,465.7	435.3	17.4	(14.5)	3,903.9
85% to 90%	402.2	22.0	2.6	(1.6)	425.2
90% to 95%	67.1	3.7	0.6	(0.4)	71.0
95% to 100%	1.1	1.3	0.6	(0.3)	2.7
> 100%	1.1	0.9	3.0	(1.4)	3.6
Unsecured loans	14.1	2.8	0.3	(1.0)	16.2
Mortgage pipeline	–	–	–	(0.1)	(0.1)
Other[1]	–	–	–	(5.1)	(5.1)
Total	39,703.4	3,549.1	206.6	(48.1)	43,411.0

Table 31 Loan to value distribution by IFRS 9 stage 2020

Notes
1. Other includes expected credit losses which are not directly attributable to underlying accounts and therefore are not allocated across loan to value bandings.

The credit quality of the mortgage book has improved, with performance being much better in 2021 than was projected at the end of 2020 when the uncertainty around the pandemic was at its highest.

The PD tables below have been updated in the year to incorporate the distribution of the Group's credit exposure by internal risk grade and their respective average PD of the Society's loans over their life (e.g. PD of less than or equal to 0.25 indicates a 0.25% chance of default over the life of the loan). These internal risk grades are used in the assessment of SICR as well as within the calculation of regulatory expected losses and capital under IRB; for more information on SICR criteria and the differences between the IFRS 9 ECL calculation and regulatory expected losses see the 2021 Accounts. Default includes cases which are three or more months in arrears or

have been three or more months in arrears at some point in the last 12 months in addition to cases which have a specified unlikeliness to pay indicator.

Loan balances are reflected in the respective PD bands of the account as modelled through the Society's standard IFRS 9 impairment models. This has led to a decrease of impairment reflected in the higher PD bands in the year as a result of the PMAs applied as a result of the Covid-19 pandemic in the prior year following application of cure rules.

For more information on PMAs see the 2021 Accounts.

As at 31 December 2021 Risk Grades	Average lifetime probability of default %	Stage 1 'Performing' £m	Stage 2 'Deteriorating' £m	Stage 3 'Default' £m	Impairment £m	Total £m
Performing						
A-C	**0.18**	**38,807.7**	**1,783.3**	**–**	**(3.0)**	**40,588.0**
D-F	**1.97**	**4,169.3**	**1,099.8**	**–**	**(3.0)**	**5,266.1**
G-J	**19.78**	**43.3**	**309.7**	**–**	**(1.2)**	**351.8**
Non-performing						
K	**39.83**	**–**	**13.7**	**–**	**(0.1)**	**13.6**
Default and possession	**100.00**	**–**	**–**	**186.7**	**(4.4)**	**182.3**
Other[1]	**N/A**	**180.5**	**19.7**	**2.3**	**(7.1)**	**195.4**
Mortgage pipeline	**N/A**	**–**	**–**	**–**	**(0.1)**	**(0.1)**
Total		**43,200.8**	**3,226.2**	**189.0**	**(18.9)**	**46,597.1**

Table 32 Lifetime probability of default by IFRS 9 stage 2021

Notes
1. Other includes equity release mortgages and other loans where credit risk is assessed using alternative calculation methods and their respective ECLs or where ECLs are not directly attributable to underlying accounts and therefore are not allocated across risk grades or to Default.

As at 31 December 2020 Risk Grades	Average lifetime probability of default %	Stage 1 'Performing' £m	Stage 2 'Deteriorating' £m	Stage 3 'Default' £m	Impairment £m	Total £m
Performing						
A-C	0.00	35,876.6	1,879.0	–	(15.9)	37,739.7
D-F	2.00	3,574.8	1,304.9	–	(9.6)	4,870.1
G-J	18.00	36.0	345.3	–	(1.9)	379.4
Non-performing						
K	33.00	–	12.3	–	(0.1)	12.2
Default and possession	100.00	–	–	202.1	(7.1)	195.0
Other[1]	N/A	216.0	7.6	4.5	(13.4)	214.7
Mortgage pipeline	N/A	–	–	–	(0.1)	(0.1)
Total		39,703.4	3,549.1	206.6	(48.1)	43,411.0

Table 33 Lifetime probability of default by IFRS 9 stage 2020

Notes
1. Other includes equity release mortgages and other loans where credit risk is assessed using alternative calculation methods and their respective ECLs or where ECLs are not directly attributable to underlying accounts and therefore are not allocated across risk grades or to Default.

5.3.9. Credit risk outlook

Headwinds persist as a result of the macroeconomic conditions (e.g. high inflation) together with ongoing risks arising from the pandemic (e.g. new variants and their downstream impacts on the economy). We therefore maintain a close watching brief and will continue to manage policy in accordance with any emerging risks.

As at 31 December 2021 we did not see any deterioration in the book as a result of the end of the furlough scheme in September 2021.

The Society's ongoing focus on low risk lending which is geographically spread across the UK continues to offer protection against future house price falls and affordability pressures.

5.4. Treasury credit risk

5.4.1. Management of treasury credit risk

The Society has a low appetite for treasury credit risk and restricts exposures to good quality counterparties with a low risk of failure.

Treasury investments in financial institutions are predominantly with highly rated UK banks, with additional credit limits extended to a small number of highly rated and systemically important institutions in Europe, Australia, Canada and the United States and multilateral development banks (MDBs). In addition, the Society invests in Covered Bonds and Residential Mortgage Backed Securities (RMBS). The treasury credit framework is reviewed annually by BRC and the Board and reflects internal analysis, external credit ratings and any other relevant factors. There is a maximum permitted exposure set for each category of investments in addition to country and regional limits.

Within the risk framework, detailed limit setting is delegated to the ALCO with oversight from the Risk function, supplemented by daily monitoring by the Treasury Credit Committee (TCC).

Exposures are reviewed continuously to ensure that they remain within the approved limits. Developments with treasury counterparties are closely monitored with detailed internal credit assessments performed annually on key counterparties with limits reduced or suspended where there are adverse changes, including changes in the creditworthiness of counterparties or markets.

Treasury assets comprise cash and balances with the Bank of England, loans and advances to credit institutions and debt securities. The majority of liquidity continues to be held in UK central bank reserves.

All of the Society's treasury exposures remain at investment grade as set out below:

As at 31 December 2021	**Aaa–Aa3 £m**	**A1–A3 £m**	**Baa1–Baa3 £m**	**Unrated £m**	**Total £m**
Central banks and sovereigns	**6,855.1**	**–**	**–**	**–**	**6,855.1**
Multilateral development banks (supranational bonds)	**157.1**	**–**	**–**	**–**	**157.1**
Financial institutions	**434.0**	**155.4**			**589.4**
Residential mortgage-backed securities	**20.4**	**–**	**–**	**–**	**20.4**
Total	**7,466.6**	**155.4**	**–**	**–**	**7,622.0**

Table 34 Treasury exposure value by rating 2021

As at 31 December 2020	Aaa–Aa3 £m	A1–A3 £m	Baa1–Baa3 £m	Unrated £m	Total £m
Central banks and sovereigns	5,979.2	–	–	–	5,979.2
Multilateral development banks (supranational bonds)	167.5	–	–	–	167.5
Financial institutions	619.3	523.1	–	–	1,142.4
Residential mortgage-backed securities	25.4	–	–	–	25.4
Total	6,791.4	523.1	–	–	7,314.5

Table 35 Treasury exposure value by rating 2020

Capital for credit risk within the liquidity book is calculated using the Standardised approach. For central banks, sovereigns, and UK Financial Institutions with a residual maturity of less than three months, risk weights prescribed in CRD IV are used. At 31 December 2021, the exposure for UK Financial Institutions with a residual maturity of less than three months was £140.8 million (2020: £372.4 million) with a capital requirement of £2.3 million (2020: £6.0 million).

For covered bonds, RMBS and other Financial Institutions the Society uses credit ratings published by Moody's. Moody's is recognised as an eligible External Credit Assessment Institution (ECAI) for this purpose. The following

table shows the exposure values and rating associated with each credit quality step. There is no credit risk mitigation applicable to these exposure values.

	Moody's rating	Risk weight %	Exposure value 2021 £m	Minimum capital requirement 2021 £m	Exposure value 2020 £m	Minimum capital requirement 2020 £m
Retail Mortgage Backed Securities (RMBS)						
Credit quality step 1	Aaa-Aa3	10	**13.9**	**0.1**	18.2	0.2
Credit quality step 1	Aaa-Aa3	20	**6.5**	**0.1**	7.2	0.1
Total RMBS			**20.4**	**0.2**	25.4	0.3
Covered bonds						
Credit quality step 1	Aaa-Aa3	10	110.6	0.9	137.4	1.1
Credit quality step 2	A1-A3	20	24.4	0.4	24.5	0.4
Total covered bonds			**135.0**	**1.3**	161.9	1.5
Financial institutions						
Credit quality step 1	Aaa-Aa3	20	**180.5**	**2.9**	87.9	1.4
Credit quality step 2	A1-A3	50	**0.1**	**0.0**	96.6	1.6
Credit quality step 3	Baa1	50	**–**	**–**	–	–
Total financial institutions			**180.6**	**2.9**	184.5	3.0
Total			**336.0**	**4.4**	371.8	4.8

Table 36 ECAI exposure values and ratings

5.4.2. Counterparty credit risk mitigation

The Society enters into derivative transactions for risk management purposes. It undertakes sale and repurchase (repo) transactions to manage liquidity and raise longer term funding, where assets such as gilts are sold with an agreement to repurchase at an agreed price on a later date. Counterparty credit risk includes the risk of default by the derivative counterparty or the risk that cash received in a repo transaction is less than the market value of the asset.

The Society manages this risk by undertaking credit assessments of all counterparties and by exchanging collateral to mitigate any exposure. Daily collateralisation of repo transactions is carried out in accordance with the Global Master Repurchase Agreements to mitigate net exposure arising from changes in market value. Similarly, all derivatives have Credit Support Annexes (CSAs) in place to ensure they are collateralised to mitigate net mark-to-market credit exposures.

The Society has entered into International Swaps and Derivatives Association (ISDA) master netting agreements for all of its derivatives (other than swaps undertaken by Coventry Building Society Covered Bond LLP and Coventry Godiva Covered Bonds LLP). These allow the Society to settle exposures 'net' in the event of a default or other predetermined event.

The Society is subject to mandatory central clearing of derivatives through a third party regulated central clearing counterparty to reduce systemic and operating risk. Under this, collateral is exchanged on a daily basis. Where the Society enters into swaps that are not currently cleared by any of the central clearing houses, e.g. cross currency swaps, these are all subject to daily exchange of collateral to better manage counterparty risk.

The Society's Covered Bond programmes (Coventry Building Society Covered Bonds LLP and Coventry Godiva Covered Bonds LLP) and Economic Master Issuer plc enter into swaps under separate ISDA agreements. Each agreement includes a CSA which provides for full collateralisation of the swap exposure with exposure thresholds in place for a single agreement before collateral is exchanged.

The £0.1 million (2020: £7.5 million) net derivative credit exposure in the table below includes £0.1 million (2020: £7.5 million) in respect of this arrangement which will only be fully collateralised if the counterparty is downgraded to below a specified credit rating.

5.4.3. Counterparty credit risk - derivatives

The balance sheet exposure values of derivative instruments are as follows. The net derivative credit exposure has reduced as a result of changes in the underlying derivative fair values during the year.

	Exposure value As at 31 December 2021 £m	Exposure value As at 31 December 2020 £m
Gross positive fair value of contracts	**406.3**	173.5
Netting benefits	**(155.6)**	(108.9)
Net credit exposure	**250.7**	64.6
Collateral held	**(250.6)**	(57.1)
Net derivative credit exposure	**0.1**	7.5

Table 37 Derivative counterparty credit exposure

As at 31 December 2021, all of the £0.1 million exposure is to Aa3 rated institutions.

The derivative exposure can only be settled net following a default or other predetermined event and therefore there is no right of set-off in the balance sheet.

For regulatory capital purposes, the Society measures derivative counterparty credit exposure values using the counterparty credit risk mark-to-market method. The net exposure value of derivatives at 31 December 2021, which includes uplifts for Potential Future Credit Exposure (PFCE) under this method, totalled £191.1 million (2020: £156.6 million).

5.4.4. Analysis of treasury assets by IFRS stage and impairment

Under IFRS 9 the calculation of impairment on treasury assets is performed on an ECL basis.

The Society determines whether there has been a significant increase in credit risk for treasury assets using a range of factors including counterparty credit ratings, internal monitoring processes and, for mortgage backed securities, stress testing. Exposures are monitored by the TCC.

All of the Society's treasury assets are assessed as stage 1 'performing' assets at both 1 January and 31 December 2021. Due to the underlying quality of the assets, they have remained resilient to the market movements caused by the impact of Covid-19.

ECLs are calculated by applying an externally published PD for the applicable credit risk rating to the treasury exposure value. The required provision has remained negligible for 2021.

As at 31 December 2021, no treasury assets were past due (2020: none).

5.4.5. Securitisation

Purchased securitisation positions

The Society's purchased securitisation positions comprise of senior tranche RMBS. The exposure values and associated risk weightings are shown in Table 36 ECAI exposure values and ratings.

Purchases and retention of RMBS are undertaken within a clearly defined credit risk policy. RMBS are predominantly held at Fair Value through Other Comprehensive Income (FVOCI) on the Society's balance sheet.

Movement on the assets value is reflected in the Society reserves and if the assets are sold before maturity, a gain or loss would be transferred to the Income Statement. RMBS are regularly reviewed in line with article 406 of the Capital Requirements Regulations, with pricing and credit conditions reviewed by the Society's TCC.

As at 31 December 2021, no purchased securitisation positions were past due or impaired (2020: none). The Society uses the Standardised approach for calculating capital requirements on its purchased securitisation positions.

Originated securitisations and Covered bonds

The Society has securitised certain mortgage loans by transferring the loans to structured entities under the Economic Master Issuer (EMI) securitisation programme and Coventry Building Society Covered Bonds LLP and Coventry Godiva Covered Bonds LLP covered bond programmes. These programmes enable the Society to obtain secured funding or to create collateral which can be used to source funding. In 2021 the Mercia and Offa securitisation programmes were closed with all mortgage loans being returned to Godiva Mortgages Limited.

The transferred mortgages remain on-balance sheet as the Society retains substantially all the risks and rewards of ownership. These assets are held at amortised cost. The structured entities are fully consolidated into the Group Accounts. The transfers of the mortgage loans to the structured entities are not treated as sales and therefore no gains or losses are recognised.

As there is not considered to be a transfer of significant credit risk, the Society does not calculate risk weighted exposure amounts for any positions it holds in the securitisations and these continue to be calculated in line with CRD IV requirements, consistent with other mortgage assets. The risk relating to the underlying mortgage pool therefore remains with the Society and is included in 'Residential mortgages' detailed throughout this document.

The Society's obligations in respect of these securitisation vehicles and programmes are limited to transferring cash flows from the underlying assets and for the covered bonds or EMI maintaining its required over-collateralisation or minimum sellers share in accordance with the rules of the programmes. The Society and its subsidiaries are under no obligation to support any losses that may be incurred by a securitisation programme or holders of the notes through a securitisation. The parties holding the notes in issue are therefore only entitled to obtain payment to the extent of the resources in the securitisation. Covered bonds in issue are direct obligations of the Society.

The securitisation vehicle and two covered bond programmes create a potential liquidity requirement for the Society due to legal covenants within the swap documentation which require the Society to post collateral with the entities under certain circumstances. The cash flows under these legal covenants are considered in the Society's internal assessment of its liquidity requirements.

If credit ratings were downgraded, the Society may need to post collateral under the EMI programme. No collateral posting was required at 31 December 2021 (2020: Nil). At 31 December 2021, the impact of a one notch credit rating downgrade would increase the required collateral to be posted by £40.0 million (2020: £9.4 million), with no further requirement for a two notch downgrade.

The Society's covered bond programmes gives rise to a similar requirement, and the Society posted collateral of £186.3 million with the Coventry Building Society Covered Bonds LLP at 31 December 2021 (2020: £50.0 million). At this point, no additional collateral would be required under a one notch or two notch downgrade; such a requirement may arise in the future dependent on the valuation of the underlying swaps. The Society was not required to post collateral with Coventry Godiva Covered Bonds LLP, but under a one notch credit rating downgrade would be required to post £38.3m (2020: Nil)

The Society provides bank account facilities to EMI and Coventry Godiva Covered Bonds LLP. Upon a one notch ratings downgrade, these facilities would need to move to a third party.

Additional information on the securitisation vehicles and covered bond programmes of the Society is contained in the 2021 Accounts.

6. Liquidity and funding risk

Liquidity risk is the risk that the Society has insufficient funds to meet its obligations as they fall due. Funding risk is the risk that the Society is unable to access funding markets or can do so only at excessive cost. Liquidity risk is difficult to eliminate, with the Society's business model transforming on-demand and relatively short-dated retail deposits to contractually much longer-term mortgage lending (maturity transformation).

6.1. Strategies and processes in the management of the liquidity risk

The Society has articulated its strategy for managing liquidity risk as:

- A clear and appropriate internally defined liquidity risk appetite which is prudent and ensures the Society remains a going concern post stress;
- A diversified funding model maintaining active retail and wholesale franchises within regulatory constraints;
- Ensuring adequate liquidity is maintained across the strategic plan;
- Maintaining a High Quality Liquid Asset portfolio, with constituent portfolios aligned to risk appetite; and
- An operational liquidity buffer to provide adequate coverage for forecasting uncertainties.

The strategy is augmented with sound risk management practices and metrics outlined within the ILAAP.

6.2. Structure and organisation of the liquidity risk management function

Funding and liquidity risks are managed on a Group basis (including all subsidiary entities) with day-to-day responsibility delegated to the CFO and Treasurer with oversight by ALCO, BRC and the Board. A sub-committee of ALCO called Liquidity Management Committee (LMC) acts as a conduit for analysis and proposals to promote detailed challenge at working level prior to any progression to ALCO. The Prudential Risk & Compliance function is responsible for oversight for liquidity risk.

6.3. Liquidity risk reporting and measurement systems

The Society maintains a range of reporting covering all aspects of cash flow and liquidity risk reporting over a variety of timeframes, including both internal and regulatory metrics, Board limits and triggers, and broader monitoring measures. A series of metrics are reported at a point-in-time as well as being forecast to monitor the impact of the business strategy on the Society's risk appetite.

6.4. Hedging and mitigating the liquidity risk

The Society holds sufficient liquidity to withstand a severe but plausible stress and operates within limits set by the Board. Furthermore, a diversified funding base is maintained to avoid any over-reliance on any funding source, type or term.

6.5. Contingency funding plans

The Society's contingency funding plan is incorporated in its Recovery Plan. The Recovery Plan includes:

- Early Warning Indicators (EWIs) and Invocation Triggers Points (ITPs) which identify risk factors that forewarn of future liquidity stress events. EWIs are particularly calibrated at an early stage so that preventative measures can be taken; although invocation of the Recovery Plan is not a requirement. The Recovery Plan includes a detailed explanation of the EWI and ITPs that are in place;

- An identified selection of available recovery options to mitigate the impact of a liquidity stress. These sources are updated and validated annually with any significant changes reported to, and agreed by, ALCO. In the event of a stress, the sources will be updated on request to support ongoing decision making;
- An analysis detailing the Society's Total Recovery Capacity, representing the maximum liquidity benefit available from deploying Recovery options in generic and specific stresses, including the secondary impact of deploying these options;
- Stress testing using a range of scenarios that trigger the deployment of Recovery option, with specific focus on the speed and extent to which these options are utilised;
- An effective plan of action to equip senior management and the Board with the most effective responses to a liquidity stress event, along with delivery of appropriate management information that is both relevant and timely;
- Clear allocation of roles and responsibility, with the names and contact details of members of the team responsible for implementation; and
- Guidance on communication with key external stakeholders so that the reputational risks of the Society can be managed.

The Recovery Plan is regularly updated and tested to ensure that it remains relevant and operationally robust.

6.6. Stress testing of liquidity risk

The Society assesses the adequacy of its liquidity resources through a process of stress testing and scenario testing. These internally defined tests complement the regulatory Liquidity Coverage Ratio, and allow the Society to prove it meets the Overall Liquidity Adequacy Rule (OLAR) as specified under the ILAAP rules.

Regular liquidity stress testing is performed and reported monthly to LMC and ALCO. The stress testing analysis is performed daily and reviewed by senior management, whilst also being incorporated into the daily liquidity risk report to evidence compliance with the Liquidity Risk Appetite. In order to identify and analyse the Society's risk exposures outside of the regular stress testing, ad hoc alternative and reverse stress testing is undertaken, with the results presented to ALCO.

The liquidity stress tests described in this section incorporate the on and off balance sheet risks of the Society's business model, with reference to the fourteen liquidity risk drivers specified under the ILAAP rules. The results of the stress tests determine the required level of liquidity the Society must hold, both on a current and forecast basis.

The structure of the stress tests is defined by the Society, and agreed as a core part of the Society's Liquidity Risk Appetite (LRA). The ILAAP and the LRA was last approved by Board in January 2021.

The liquidity risk drivers detailed in the ILAAP rules are set out below. In this section, the assumptions used in the Society's assessment of these risk drivers are set out. These assumptions have been previously approved by ALCO and BRC, and form part of the ILAAP document and process approved by Board.

The ILAAP rules require the Society to undertake stress testing based on three scenarios:

- Firm-Specific stress;
- Market-Wide stress; and
- Combined stress.

The Combined stress test is the most severe of these three tests and is currently used within the Society's LRA for all periods (7, 30 and 90 day stress).

The Combined liquidity stress models the simultaneous impact of a:

- Firm-Specific stress – an unforeseen Society specific liquidity stress event affecting both wholesale lenders and retail depositors. This results in large retail withdrawals in the short-term and a lowered ability to raise new funding. A higher volume of maturing wholesale deposits are required to be repaid, and the Society's rating is impacted by two notches from both rating agencies, triggering additional contractual liquidity requirements; and
- Market-Wide stress – an unforeseen sector-wide liquidity stress which indirectly affects the Society. This is characterised by increased risk concerns amongst market participants and (less so) in retail depositors. Wholesale rollover is reduced as other market participants become more risk averse. This impairs the requirement to raise liquidity from the existing liquidity portfolio leading to increased collateral haircuts. Retail depositors also look to spread funds across a number of deposit takers to maximise their FSCS coverage but would not seek to take savings out of the system altogether. The scenario is cognisant of developments in the FSCS scheme since 2008, and in the Bank of England sterling monetary framework.

The Combined stress takes the Society's latest liquidity position and calculates the survival period after applying all elements of the stress. Survival under this stress scenario is defined as:

- Holding sufficient cash to meet both the outflows of the first 7 days and the stressed intra-day liquidity requirement;
- Holding sufficient HQLA to meet the outflows of the first 30 days of a stress plus the survival point at the end of the 30 days; and
- Total liquidity resources to meet further outflows up to a 90 day horizon and to meet the survival point at the end of this period.

In addition to these stresses, the Society uses an additional permanent stress scenario and a variety of different scenarios. These scenarios are devised by considering prevailing market conditions/challenges, or to specifically stretch the Society's capabilities and resources based on risk identification and monitoring exercises.

See additional information on Liquidity and Funding risk within the Risk Management Report in the 2021 Accounts.

7. Operational risk

7.1. Introduction

Operational risk is defined as the risk of loss resulting from inadequate or failed internal processes, people and systems or from external events. The Society manages operational risks with the objectives of protecting members' interests and keeping the Society safe and secure.

7.2. Strategies and processes to manage operational risk

The Operational Risk Management Framework (ORMF) forms part of the wider ERMF. The ERMF explains how the component parts of the framework come together to enable the Society to identify and effectively manage all of its risks. The Society's high level risk strategy is defined in the ERMF.

The Society's ORMF has an Operational Risk Policy and Risk Management procedures to support the consistent, effective and timely identification, assessment, control, monitoring and reporting of operational risks and events.

The Society operates a Risk and Control Self-Assessment (RCSA) process. RCSA owners are required to:

- Identify and assess the potential impacts of risks on an inherent and residual basis;
- Regularly test the effectiveness of controls; and
- Develop and implement action plans to address control weaknesses.

For risks that are rated Amber or Red, RCSA owners must either take remedial actions to reduce the risks, or accept the risk where remedial action is either not possible or appropriate due to practical or cost considerations. Operational risk events with a 'Minor' or above impact are recorded and control gaps identified and remediated. Operational risks and events that are rated Amber or Red are reported to the Operational Risk Committee (ORC) with Red items also reported to BRC.

The Operational Risk Appetite Statement defines the amount of risk that the Society is willing to accept. Operational risk sub-category owners are responsible for:

- Defining risk appetite for their sub-risk category; and
- Ensuring that a comprehensive and up-to-date risk dashboard, incorporating Key Risk indicators, is reported to ORC on a monthly basis.

7.3. Structure and organisation of the operational risk management function

The Society has adopted the 'three lines of defence' approach to the management of operational risks:

1. Under the first line of defence, operational management has responsibility for owning, assessing, managing and mitigating risks;
2. The second line of defence provides advice, independent oversight and challenge to the management of those risks; and
3. The third line provides independent assurance.

Operational risk is managed, reported and controlled across a number of sub-categories, consistent with the Basel risk classifications, industry best practice and the Society's business model.

The management of Operational Risk is overseen by ORC, which provides primary oversight of all operational risk categories with further oversight provided by BRC and the Board.

7.4. Operational risk measurements

The Society uses the standardised approach for calculating its Pillar 1 capital requirement for operational risk. The calculation uses net interest income averaged over a three year period. The operational risk capital requirement in the year to 2021 was £635.8 million (2020: £605.4 million). The reduction in capital requirement is a result of continuation of low mortgage pricing combined with the Society's strategy of paying the best possible interest rates to its saving members.

7.5. Mitigating for operational risk

The ORMF describes the Society's approach to the management of Operational risk including the definition of control framework requirements by category.

See additional information on Operational risk within the Risk Management Report in the 2021 Accounts.

Appendix 1. EBA own funds disclosure template

Any blank lines in the template have been removed.

		Transitional CRD IV		End-point CRD IV	
		2021	2020	**2021**	2020
		£m	£m	**£m**	£m
Common Equity Tier 1 (CET 1) Capital: instruments and reserves					
2	Retained earnings	**2,012.6**	1,835.1	**2,012.6**	1,835.1
3	Accumulated other comprehensive income (and other reserves)	**32.0**	(44.0)	**32.0**	(44.0)
5a	Independently reviewed interim profits net of any foreseeable charge or dividend	**(10.4)**	(10.4)	**(10.4)**	(10.4)
6	Common Equity Tier 1 (CET 1) capital before regulatory adjustments	**2,034.2**	1,780.7	**2,034.2**	1,780.7
Common Equity Tier 1 (CET 1) capital: regulatory adjustments					
7	Additional value adjustments (negative amount)	**(0.7)**	(1.0)	**(0.7)**	(1.0)
8	Intangible assets (net of related deferred tax liability (negative amount)	**(32.9)**	(31.0)	**(32.9)**	(31.0)
11	Fair value reserves related to gains or losses on cash flow hedges	**(27.5)**	46.3	**(27.5)**	46.3
12	Negative amounts resulting from the calculation of expected loss amounts	**(31.4)**	(4.0)	**(31.4)**	(4.0)
15	Defined-benefit pension fund assets (negative amount)	**(19.9)**	(7.7)	**(19.9)**	(7.7)
27a	Other regulatory adjustments to CET 1 capital (including IFRS 9 transitional adjustments when relevant)	**2.4**	0.4	**–**	–
28	Total regulatory adjustments to Common Equity Tier 1 (CET 1)	**(110.0)**	3.0	**(112.4)**	2.6
29	Common Equity Tier 1 (CET 1) capital	**1,924.2**	1,783.7	**1,921.8**	1,783.3
Additional Tier 1 (AT 1) capital: instruments					
30	Capital instruments and the related share premium accounts	**415.0**	415.0	**415.0**	415.0
31	of which: classified as equity under applicable accounting standards	**415.0**	415.0	**415.0**	415.0
33	Amount of qualifying items referred to in Article 484 (4) and the related share premium accounts subject to phase out from AT 1	**16.0**	32.0	**–**	–
36	Additional Tier 1 (AT 1) capital before regulatory adjustments	**431.0**	447.0	**415.0**	415.0
44	Additional Tier 1 (AT 1) capital	**431.0**	447.0	**415.0**	415.0
45	Tier 1 capital (T1 = CET 1 + AT 1)	**2,355.2**	2,230.7	**2,336.8**	2,198.3

		Transitional CRD IV		End-point CRD IV	
		2021 £m	**2020 £m**	**2021 £m**	**2020 £m**
Tier 2 (T2) capital: instruments and provisions					
47	Amount of qualifying items referred to in Article 484 (5) and the related share premium accounts subject to phase out from T2	**5.5**	11.1	**–**	–
51	Tier 2 (T2) capital before regulatory adjustments	**5.5**	11.1	**–**	–
58	Tier 2 (T2) capital	**5.5**	11.1	**–**	–
59	Total capital (TC = T1 + T2)	**2,360.7**	2,241.8	**2,336.8**	2,198.3
60	Total risk weighted assets	**5,305.5**	5,410.9	**5,303.6**	5,410.6
Capital ratios and buffers					
61	Common Equity Tier 1 (as a percentage of total risk exposure amount)	**36.3%**	33.0%	**36.2%**	33.0%
62	Tier 1 (as a percentage of total risk exposure amount)	**44.4%**	41.2%	**44.1%**	40.6%
63	Total capital (as a percentage of total risk exposure amount)	**44.5%**	41.4%	**44.1%**	40.6%
64	Institution specific buffer requirement (CET 1 requirement in accordance with article 92 (1) (a) plus capital conservation and countercyclical buffer requirements, plus systemic risk buffer, plus systemically important institution buffer expressed as a percentage of risk exposure amount)	**7.0%**	7.0%	**7.0%**	7.0%
65	of which: capital conservation buffer requirement	**2.5%**	2.5%	**2.5%**	2.5%
66	of which: countercyclical buffer requirement	**0.0%**	0.0%	**0.0%**	0.0%
68	Common Equity Tier 1 available to meet buffers (as a percentage of risk exposure amount)	**31.8%**	28.5%	**31.7%**	28.5%
Capital instruments subject to phase-out arrangements (only applicable between 1 Jan 2014 and 1 Jan 2022)					
82	Current cap on AT 1 instruments subject to phase out arrangements	**16.0**	32.0	**–**	–
83	Amount excluded from AT 1 due to cap (excess over cap after redemptions and maturities)	**24.0**	8.0	**–**	–
84	Current cap on T2 instruments subject to phase out arrangements	**5.5**	11.1	**–**	–
85	Amount excluded from T2 due to cap (excess over cap after redemptions and maturities	**9.5**	13.9	**–**	–

Table 38 EBA own funds disclosure template

Appendix 2. **Capital instruments key features**

1	Issuer	Coventry	Coventry	Coventry (Stroud & Swindon)
2	ISIN	XS1961836712	GB0002290764	N/a
2a	Public or private placement	Public	Public	Private
3	Gov. law (sub)	English	English	English
3a	Contractual recognition of write down and conversion powers of resolution authorities	Yes	No	No
	Regulatory treatment			
4	Transitional CRR rules	AT 1	AT 1	T2
5	Post-transitional CRR rules	AT 1	Ineligible	Ineligible
6	Eligible at Group (G), Individual Consolidated (IC) or Society (S)	G; IC; S	G; IC; S	G; IC; S
7	Instrument type (types to be specified by each jurisdiction)	Perpetual Capital Security	PIBS	Sub Debt
8	Regulatory capital value (£m)	415,000,000	16,000,000	5,548,300
9	Nominal amount of instrument	415,000,000	40,000,000	15,000,000
9a	Issue price	100	100.749	100
9b	Redemption price	100	100	100
10	Accounting classification	Shareholders' equity	Liability - amortised cost	Liability - amortised cost
11	Original date of issuance	02-Apr-19	28-May-92	23-Aug-01
12	Perpetual or dated	Perpetual	Perpetual	Dated
13	Original maturity date	No maturity	No maturity	23-Aug-32
14	Issuer call	Yes	N/a	Yes
15	Optional call date, contingent call dates and redemption amount	18-Sep-24; par regulatory/tax call	N/a	23-Aug-27
16	Subsequent call dates, if applicable	5 yearly	N/a	N/a
	Coupons / dividends			
17	Fixed or floating dividend/coupon	Fixed	Fixed	Fixed
18	Coupon rate and any related index	6.875%	12.125%	7.540%
19	Existence of a dividend stopper	No	No	No
20a/b	Fully discretionary, partially or mandatory (in terms of timing)	Fully discretionary	Partially discretionary	Mandatory
21	Existence of step up or other incentive to redeem	No	No	Yes
22	Non-cumulative or cumulative	Non-cumulative	Non-cumulative	N/a

23	Convertible or non-convertible	Convertible	Non-convertible	Non-convertible
24	If convertible, conversion trigger(s)	Contractual – CET 1 <7%	N/a	N/a
25	If convertible, fully or partially	Fully	N/a	N/a
26	If convertible, conversion rate	One for every £67 held	N/a	N/a
27	If convertible, mandatory or optional conversion	Mandatory	N/a	N/a
28	Specify output instrument	CCDS	N/a	N/a
29	Specify issuer of output instrument	Coventry	N/a	N/a
30	Write-down features	Contractual: none; statutory: via bail-in	Contractual: none; statutory: via bail-in	Contractual: none; statutory: via bail-in
31-34	If w/d, trigger(s), full/partial, PWD/TWD	N/a	N/a	N/a
35	Instrument type immediately senior	Sub Debt	Sub Debt	Senior Unsecured
36	Non-compliant transitioned features	No	Yes	Yes
37	If yes, specify non-compliant features	N/a	No contractual write-down or conversion	Step-up reset rate

Table 39 Capital instruments key features

Further information on Perpetual Capital Securities and PIBS is available on the Society's website (www.coventrybuildingsociety.co.uk). Further information on the immaterial Tier 2 subordinated debt is available on request.

Appendix 3. **Asset encumbrance disclosure template**

Encumbered assets are those which are pledged or otherwise committed to counterparties to secure, collateralise or credit-enhance a transaction, such that the assets cannot be freely transferred, withdrawn, liquidated, sold or disposed. The counterparties to which the assets are pledged, such as secured creditors, have prior claim on encumbered assets in the event of insolvency. The Society manages encumbrance in line with standard market practice and as set out in the legal documentation of any secured funding programmes.

The Society's assets are encumbered primarily through secured wholesale issuances (Covered Bond and RMBS) as well as through repurchase agreements and utilisation of Bank of England funding facilities including the Term Funding Scheme with additional incentives for SMEs (TFSME) and Open Market Operations (OMO). The Society has both debt securities and residential mortgage loans encumbered as part of secured funding transactions. In addition the Society has assets encumbered CSAs accounts as a result of derivative transactions.

The Society has £2,250m of retained Covered Bonds in the Coventry Building Society Covered Bonds LLP, £2,000m of retained Covered Bonds in Godiva Covered Bonds LLP and £367m of retained securitisations, some of which are encumbered with the Bank of England. Covered Bonds are also partially retained and encumbered for OCIR. For retained issuances the Society reports encumbrance of the underlying mortgage assets rather than the retained notes (a 'look through' approach).

Certain cash/assets related to the Special Purpose Vehicles (SPVs) are also considered encumbered, including cash in external bank account providers which includes mortgage receipts yet to pay down via the waterfall as well as cash/assets posted as collateral due to ratings deterioration as outlined in the transaction documents. No matching liability is reported against this encumbrance.

The Society's UK Consolidation Group includes SPV Economic Master Issuer and two Covered Bond related entities: Coventry Building Society Covered Bonds LLP and Coventry Godiva Covered Bonds LLP.

The Society only has Sterling denominated encumbered assets, collateral and off-balance sheet items and sources of encumbrance.

As at 31 December 2021 the Society reported £39,427.2m of unencumbered assets, of which £300.4m the Society would not deem available for encumbrance in the normal course of its business.

The Society has no differences between the regulatory consolidation scope used for the purpose of the disclosures on asset encumbrance and the scope retained for the application of the liquidity requirements on a consolidated basis which is used to define (E)HQLA (Extremely High Quality Liquid Assets) eligibility.

There are no differences between:

1. pledged and transferred assets in accordance with the applicable accounting frameworks and as applied by the institution; and
2. encumbered assets and an indication of any difference of treatment of transactions, such as when some transactions are deemed to lead to pledge or transfer of assets but not to encumbrance of assets, or vice versa.

The exposure values used for the purposes of these disclosures are those as at 31 March 2021, 30 June 2021, 30 September 2021 and 31 December 2021. The median values for the year have been derived by arranging these quarter end values in order of size and taking the mean of the middle two values.

A general description of the terms and conditions of the collateralisation agreements entered into for securing liabilities are available in the 2021 Accounts.

2021		Carrying amount of encumbered assets **£m**	of which notionally eligible EHQLA and HQLA **£m**	Fair value of encumbered assets **£m**	of which notionally eligible EHQLA and HQLA **£m**	Carrying amount of unencumbered assets **£m**	of which notionally eligible EHQLA and HQLA **£m**	Fair value of unencumbered assets **£m**	of which notionally eligible EHQLA and HQLA **£m**
010	Assets of the reporting institution	**15,161.8**	**155.2**			**38,283.0**	**586.1**		
030	Equity instruments	**–**	**–**			**5.0**	**–**		
040	Debt securities	**155.2**	**155.2**	**155.2**	**155.2**	**592.9**	**586.1**	**593.0**	**586.5**
050	of which: covered bonds	**–**	**–**	**–**	**–**	**148.3**	**148.3**	**148.7**	**148.7**
060	of which: asset backed securities	**–**	**–**	**–**	**–**	**22.1**	**15.3**	**21.8**	**15.3**
070	of which: issued by general government	**155.2**	**155.2**	**155.2**	**155.2**	**274.5**	**274.5**	**274.5**	**274.5**
080	of which: issued by financial corporations	**–**	**–**	**–**	**–**	**325.3**	**318.6**	**325.0**	**318.6**
120	Other assets[1]	**15,015.4**	**0.0**			**37,610.2**	**–**		

Table 40 Encumbered and unencumbered assets 2021

Notes
1. All remaining balance sheet assets, predominantly loans and advances to customers.

2020		Carrying amount of encumbered assets £m	of which notionally eligible EHQLA and HQLA £m	Fair value of encumbered assets £m	of which notionally eligible EHQLA and HQLA £m	Carrying amount of unencumbered assets £m	of which notionally eligible EHQLA and HQLA £m	Fair value of encumbered assets £m	of which notionally eligible EHQLA and HQLA £m
010	Assets of the reporting institution	14,337.8	105.9			36,056.9	5,459.5		
030	Equity instruments	–	–			4.1	–		
040	Debt securities	105.9	105.9	105.9	105.9	898.3	890.9	898.6	891.7
050	of which: covered bonds	–	–	–	–	187.2	187.2	188.1	188.1
060	of which: asset backed securities	–	–	–	–	26.2	18.8	25.5	18.8
070	of which: issued by general government	105.9	105.9	105.9	105.9	528.7	528.7	528.7	528.7
080	of which: issued by financial corporations	–	–	–	–	26.2	18.8	25.5	18.8
120	Other assets[1]	14,100.3	–			35,075.9	4,511.8		

Table 41 Encumbered and unencumbered assets 2020

Notes

1. All remaining balance sheet assets, predominantly loans and advances to customers.

Collateral received

The EBA Guidelines allow competent authorities to waive the requirement to disclose Collateral received and in Supervisory Statement SS 6/17 the PRA waived the requirement subject to a firm meeting certain criteria. The Society meets the criteria and therefore Collateral received is not disclosed.

Carrying amount of selected financial liabilities

2021		**Matching liabilities, contingent liabilities or securities lent £m**	**Assets, collateral received and own debt securities issued other than covered bonds and ABSs encumbered £m**
		010	**030**
010	**Carrying amount of selected financial liabilities**	**9,174.3**	**14,693.7**

Table 42 Encumbered assets/collateral received and associated liabilities 2021

2020			
010	Carrying amount of selected financial liabilities	9,420.9	13,751.8

Table 43 Encumbered assets/collateral received and associated liabilities 2020

Over collateralisation

The levels of over collateralisation that the Society posts varies across transactions based on a series of factors including the instrument rating, the regulated status, the structure and risks borne/resulting from the transaction, and the term. The level of over collateralisation incurred in the course of business as usual and in stress is managed and modelled on a daily basis by the Society, which can impact the choice of funding instruments utilised, the form of assets pledged to meet collateral calls, and the channel by which assets are (or are assumed to be) monetised.

The Society is over collateralised in respect of both covered bond programmes, its securitisation programme, its over-the-counter derivatives, its repurchase agreements and through Bank of England funding facilities (TFSME). As at 31 December 2021, the Society is over collateralised to the extent shown in the table below:

Source of encumbrance	Over-collateralisation £m
Over-the-counter derivatives	424.6
Repurchase agreements	404.8
BoE Funding Facilities	3,112.3
Covered bonds securities issued	1,428.1
Asset-backed securities issued	56.5
Other	436.5
Total	**5,862.8**

Table 44 Over-collateralisation

Appendix 4. **Leverage ratio disclosure templates**

		Applicable Amount	
		2021	2020
		£m	£m
1	Total assets as per published financial statements	**54,529.7**	51,498.3
4	Adjustments for derivative financial instruments	**(141.5)**	27.8
5	Adjustments for securities financing transactions "SFTs"	**74.5**	76.1
6	Adjustment for off-balance sheet items (i.e. conversion to credit equivalent amounts of off-balance sheet exposures)	**429.0**	515.7
7	Other adjustments	**(92.4)**	(429.7)
8	**Total leverage exposure**	**54,799.3**	51,688.2

Table 45 Summary reconciliation of accounting assets and leverage ratio exposure

		CRR leverage ratio exposures	
		2021	2020
		£m	£m
	On-balance sheet exposures (excluding derivatives and SFTs)		
1	On-balance sheet items (excluding derivatives, SFTs and fiduciary assets, but including collateral)	**54,120.1**	51,321.6
2	(Asset amounts deducted in determining Tier 1 capital)	**(84.9)**	(43.7)
3	**Total on-balance sheet exposures (excluding derivatives, SFTs and fiduciary assets) (sum of lines 1 and 2)**	**54,035.2**	51,277.9
	Derivative exposures		
4	Replacement cost associated with all derivatives transactions (i.e. net of eligible cash variation margin)	**0.1**	64.6
5	Add-on amounts for PFE associated with all derivatives transactions (mark-to-market method)	**264.7**	136.7
7	(Deductions of receivables assets for cash variation margin provided in derivatives transactions)	**(4.2)**	(382.8)
11	**Total derivative exposures (sum of lines 4 to 10)**	**260.6**	(181.5)
	Securities financing transaction exposures		
14	Counterparty credit risk exposure for SFT assets	**74.5**	76.1
16	**Total securities financing transaction exposures (sum of lines 12 to 15a)**	**74.5**	76.1
	Other off-balance sheet exposures		
17	Off-balance sheet exposures at gross notional amount	**2,105.7**	2,534.0
18	(Adjustments for conversion to credit equivalent amounts)	**(1,676.7)**	(2,018.3)
19	**Other off-balance sheet exposures (sum of lines 17 to 18)**	**429.0**	515.7
	Capital and total exposures		
20	Tier 1 capital	**2,336.8**	2,198.3
21	**Total leverage ratio exposures (sum of lines 3, 11, 16, 19, EU-19a and EU-19b)**	**54,799.3**	51,688.2
	Leverage ratio		
22	**CRR Leverage ratio**	**4.3%**	4.3%
22A	**UK Leverage ratio**	**4.8%**	4.6%
	Choice on transitional arrangements and amount of derecognised fiduciary items		
EU-23	Choice on transitional arrangements for the definition of the capital measure	Fully phased in	Fully phased in

Table 46 Leverage ratio common disclosures

Details of the differences between the UK Leverage ratio and the CRR Leverage ratio are described in Section 3.4 Leverage ratio.

		CRR leverage ratio exposures	
		2021	2020
		£m	£m
EU-1	Total on-balance sheet exposures (excluding derivatives, SFTs, and exempted exposures), of which:	**54,120.1**	51,321.6
EU-3	Banking book exposures, of which:	**54,120.1**	51,321.6
EU-4	Covered bonds	**135.2**	162.1
EU-5	Exposures treated as sovereigns	**6,855.0**	5,979.2
EU-6	Exposures to regional governments, MDB, international organisations and PSE not treated as sovereigns	**157.1**	167.5
EU-7	Institutions	**432.8**	960.1
EU-8	Secured by mortgages of immovable properties	**46,295.3**	43,826.0
EU-9	Retail exposures	**13.5**	16.2
EU-10	Corporate	**0.9**	–
EU-11	Exposures in default (standardised)	**15.5**	6.8
EU-12	Other exposures (e.g. equity, securitisations, and other non-credit obligation assets)	**214.8**	203.7

Table 47 Split-up of on-balance sheet exposures (excluding derivatives, SFTs and exempt exposures)

Appendix 5. **Countercyclical capital buffers disclosure templates**

The countercyclical buffer is an additional requirement introduced by CRD IV, calculated by applying a weighted average of country countercyclical buffer rates based on the geographical distribution of relevant exposures to the overall capital requirements of the Society. The following templates disclose information relevant for the calculation of the countercyclical buffer as at 31 December 2021 in accordance with Regulation (EU) 2015/1555 on a consolidated basis.

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

2021		General credit exposures		Trading book exposures		Securitisation exposures		Own funds requirements					
Row		Exposure value for SA	Exposure value for IRB	Sum of long and short positions of trading book	Value of trading book exposures for internal models	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total	Own fund requirement weights	Countercyclical capital buffer rate
		010	020	030	040	050	060	070	080	090	100	110	120
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	Weighting	%
010	**Breakdown by country**												
	UK	**591.5**	**48,461.3**	**–**	**–**	**20.4**	**–**	**362.6**	**–**	**0.2**	**362.8**	**1.0**	**0%**
020	**Total**	**591.5**	**48,461.3**	**–**	**–**	**20.4**	**–**	**362.6**	**–**	**0.2**	**362.8**	**1.0**	**0%**

Table 48 Geographical distribution of credit exposures 2021

2020		General credit exposures		Trading book exposures		Securitisation exposures		Own funds requirements					
Row		Exposure value for SA	Exposure value for IRB	Sum of long and short positions of trading book	Value of trading book exposures for internal models	Exposure value for SA	Exposure value for IRB	Of which: General credit exposures	Of which: Trading book exposures	Of which: Securitisation exposures	Total	Own fund requirement weights	Countercyclical capital buffer rate
		010	020	030	040	050	060	070	080	090	100	110	120
		£m	£m	£m	£m	£m	£m	£m	£m	£m	£m	Weighting	%
010	Breakdown by country												
	UK	640.2	46,378.5	–	–	25.4	–	371.1	–	0.3	371.4	1.0	0%
020	Total	640.2	46,378.5	–	–	25.4	–	371.1	–	0.3	371.4	1.0	0%

Table 49 Geographical distribution of credit exposures 2020

Row		2021 Column	2020 Column
		010	010
010	**Total risk exposure amount**	**£5,305.5m**	£5,410.9m
020	**Institution specific countercyclical buffer rate**	**0%**	0%
030	**Institution specific countercyclical buffer requirement**	**–**	–

Table 50 Amount of institution specific countercyclical capital buffer

Appendix 6. **Non-performing and forborne exposures**

The Society's non-performing and forborne exposures are only associated to its loans and advances. During the year the Society reviewed its classification of forborne exposures and has increased the breadth of concessions included. These movements have been explained within Section 5.3.2 The Society's approach to payment difficulties.

2021		**Gross carrying amount/nominal amount of exposures with forbearance measures**				**Accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions**		**Collateral received and financial guarantees received on forborne exposures**	
			Non-performing forborne						
Row		**Performing forborne £m**	**£m**	**Of which defaulted £m**	**Of which impaired £m**	**On performing forborne exposures £m**	**On non-performing forborne exposures £m**	**£m**	**Of which collateral and financial guarantees received on non-performing exposures with forbearance measures £m**
1	**Loans and advances**	**78.2**	**38.1**	**32.5**	**32.7**	**0.0**	**0.3**	**116.0**	**37.8**
7	***Households***	**78.2**	**38.1**	**32.5**	**32.7**	**0.0**	**0.3**	**116.0**	**37.8**
9	**Loan commitments given**	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
10	***Total***	**78.2**	**38.1**	**32.5**	**32.7**	**0.0**	**0.3**	**116.0**	**37.8**

Table 51 Credit quality of forborne exposures 2021

2020		Gross carrying amount/nominal amount of exposures with forbearance measures				Accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions		Collateral received and financial guarantees received on forborne exposures	
			Non-performing forborne						
Row		Performing forborne £m	£m	Of which defaulted £m	Of which impaired £m	On performing forborne exposures £m	On non-performing forborne exposures £m	£m	Of which collateral and financial guarantees received on non-performing exposures with forbearance measures £m
1	Loans and advances	7.7	2.1	0.4	1.1	–	–	9.8	2.1
7	*Households*	7.7	2.1	0.4	1.1	–	–	9.8	2.1
9	Loan commitments given	0.1	–	–	–	–	–	0.1	–
10	*Total*	7.8	2.1	0.4	1.1	–	–	9.9	2.1

Table 52 Credit quality of forborne exposures 2020

2021

Row		Gross carrying amount/nominal amount											
		Performing exposures			**Non-performing exposures**								
		£m	**Not past due or past due ≤ 30 days £m**	**Past due > 30 days ≤ 90 days £m**	**£m**	**Unlikely to pay that are not past due or are past due ≤ 90 days £m**	**Past due > 90 days ≤ 180 days £m**	**Past due > 180 days ≤ 1 year £m**	**Past due > 1 year ≤ 2 years £m**	**Past due > 2 years ≤ 5 years £m**	**Past due > 5 years ≤ 7 years £m**	**Past due > 7 years £m**	**Of which defaulted £m**
1	**Loans and advances**	**46,444.6**	**46,354.3**	**90.4**	**194.8**	**117.8**	**39.5**	**19.9**	**13.8**	**3.8**	**–**	**–**	**180.2**
6	***Non-financial corporations***	**1.0**	**1.0**	**–**	**0.3**	**0.3**	**–**	**–**	**–**	**–**	**–**	**–**	**0.3**
7	***Of which SMEs***	**1.0**	**1.0**	**–**	**0.3**	**0.3**	**–**	**–**	**–**	**–**	**–**	**–**	**0.3**
8	***Households***	**46,443.6**	**46,353.3**	**90.4**	**194.5**	**117.5**	**39.5**	**19.9**	**13.8**	**3.8**	**–**	**–**	**179.9**
15	**Off-balance-sheet exposures**	**2,105.5**			**0.3**								**0.2**
21	***Households***	**2,105.5**			**0.3**								**0.2**
22	***Total***	**48,550.1**	**46,354.3**	**90.4**	**195.1**	**117.8**	**39.5**	**19.9**	**13.8**	**3.8**	**–**	**–**	**180.4**

Table 53 Credit quality of performing and non-performing exposures by past due days 2021

2020

Row		Gross carrying amount/nominal amount											
		Performing exposures			Non-performing exposures								
		£m	Not past due or past due ≤ 30 days £m	Past due > 30 days ≤ 90 days £m	£m	Unlikely to pay that are not past due or are past due ≤ 90 days £m	Past due > 90 days ≤ 180 days £m	Past due > 180 days ≤ 1 year £m	Past due > 1 year ≤ 2 years £m	Past due > 2 years ≤ 5 years £m	Past due > 5 years ≤ 7 years £m	Past due > 7 years £m	Of which defaulted £m
1	Loans and advances	43,252.5	43,171.5	81.1	206.6	128.6	36.6	27.2	10.8	3.1	0.2	0.1	206.6
6	*Non-financial corporations*	1.4	1.4	–	0.4	0.4	–	–	–	–	–	–	0.4
7	*Of which SMEs*	1.4	1.4	–	0.4	0.4	–	–	–	–	–	–	0.4
8	*Households*	43,251.1	43,170.1	81.1	206.2	128.2	36.6	27.2	10.8	3.1	0.2	0.1	206.2
15	Off-balance-sheet exposures	2,541.9			0.4								–
21	*Households*	2,541.9			0.4								–
22	*Total*	45,794.4	43,171.5	81.1	207.0	128.6	36.6	27.2	10.8	3.1	0.2	0.1	206.6

Table 54 Credit quality of performing and non-performing exposures by past due days 2020

2021		Gross carrying amount/nominal amount						Accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions						Accumulated partial write-off	Collateral and financial guarantees received	
		Performing exposures			Non-performing exposures			Performing exposures – accumulated impairment and provisions			Non-performing exposures – accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions					
Row		£m	Of which stage 1 £m	Of which stage 2 £m	£m	Of which stage 2 £m	Of which stage 3 £m	£m	Of which stage 1 £m	Of which stage 2 £m	£m	Of which stage 2 £m	Of which stage 3 £m	£m	On performing exposures £m	On non-performing exposures £m
1	Loans and advances	46,444.6	43,222.5	3,222.1	194.8	5.7	189.1	(12.5)	(3.6)	(8.9)	(6.3)	(0.1)	(6.2)	–	46,326.0	189.8
6	*Non-financial corporations*	*1.0*	–	*1.0*	*0.3*	–	*0.3*	*(0.1)*	–	*(0.1)*	*(0.1)*	-	*(0.1)*	–	*0.9*	*0.2*
7	*Of which SMEs*	*1.0*	–	*1.0*	*0.3*	–	*0.3*	*(0.1)*	–	*(0.1)*	*(0.1)*	-	*(0.1)*	–	*0.9*	*0.2*
8	*Households*	*46,443.6*	*43,222.5*	*3,221.1*	*194.5*	*5.7*	*188.8*	*(12.4)*	*(3.6)*	*(8.8)*	*(6.2)*	*(0.1)*	*(6.1)*	–	*46,325.1*	*189.6*
15	Off-balance-sheet exposures	2,105.5	2,096.9	8.6	0.3	–	0.3	–	–	–	–	–	–		24.7	0.2
21	*Households*	*2,105.5*	*2,096.9*	*8.6*	*0.3*	–	*0.3*	–	–	–	–	–	–		*24.7*	*0.2*
22	Total	48,550.1	45,319.4	3,230.7	195.1	5.7	189.4	(12.5)	(3.6)	(8.9)	(6.3)	(0.1)	(6.2)	–	46,350.7	190.0

Table 55 Performing and non-performing exposures and related provisions 2021

2020		Gross carrying amount/nominal amount						Accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions						Accumulated partial write-off	Collateral and financial guarantees received	
		Performing exposures			Non-performing exposures			Performing exposures – accumulated impairment and provisions			Non-performing exposures – accumulated impairment, accumulated negative changes in fair value due to credit risk and provisions					
Row		£m	Of which stage 1 £m	Of which stage 2 £m	£m	Of which stage 2 £m	Of which stage 3 £m	£m	Of which stage 1 £m	Of which stage 2 £m	£m	Of which stage 2 £m	Of which stage 3 £m	£m	On performing exposures £m	On non-performing exposures £m
1	Loans and advances	43,252.5	39,703.4	3,549.1	206.6	–	206.6	(36.9)	(8.5)	(28.4)	(11.1)	–	(11.1)	–	43,145.5	198.4
6	*Non-financial corporations*	*1.4*	–	*1.4*	*0.4*	–	*0.4*	*(0.2)*	–	*(0.2)*	*(0.2)*	–	*(0.2)*	–	*1.2*	*0.2*
7	*Of which SMEs*	*1.4*	–	*1.4*	*0.4*	–	*0.4*	*(0.2)*	–	*(0.2)*	*(0.2)*	–	*(0.2)*	–	*1.2*	*0.2*
8	*Households*	*43,251.1*	*39,703.4*	*3,547.7*	*206.2*	–	*206.2*	*(36.7)*	*(8.5)*	*(28.2)*	*(10.9)*	–	*(10.9)*	–	*43,144.3*	*198.2*
15	Off-balance-sheet exposures	2,541.9	2,532.2	9.7	0.4	–	0.4	–	–	–	–	–	–		27.4	0.3
21	*Households*	*2,541.9*	*2.532.2*	*9.7*	*0.4*	–	*0.4*	–	–	–	–	–	–		*27.4*	*0.3*
22	Total	45,794.4	42,235.6	3,558.8	207.0	–	207.0	(36.9)	(8.5)	(28.4)	(11.1)	–	(11.1)	–	43,172.9	198.7

Table 56 Performing and non-performing exposures and related provisions 2020

		2021		2020	
		Collateral obtained by taking possession		Collateral obtained by taking possession	
		Value at initial recognition £m	**Accumulated negative changes £m**	Value at initial recognition £m	Accumulated negative changes £m
3	*Residential immovable property*	**0.0**	**0.0**	3.4	0.4
8	***Total***	**0.0**	**0.0**	3.4	0.4

Table 57 Collateral obtained by taking possession and execution processes

Appendix 7. Liquidity Coverage Ratio (LCR) disclosures

In accordance with the PRA Rulebook this Appendix sets out the Liquidity Coverage Ratio (LCR) disclosures in the format prescribed under CRR. The LCR is a measure which aims to ensure that an entity maintains an adequate level of liquidity to meet its needs for a 30 day period under severe stress conditions. These disclosures complement the disclosure of liquidity risk management under the CRR which are included in section 6 and within the 2021 Accounts Risk Management Report.

The main drivers of LCR results

The retail deposits are the main driver in the LCR requirement, representing over 61% of the total stressed outflows. Periodic changes in the retail requirement typically result from the maturity of term deposits falling into the LCR stress window. Mortgage pipeline and wholesale funding combine to account for 30% of the Society's remaining liquidity requirement, an increase on 2020 largely driven by a larger volume of short term wholesale funding.

Explanations on the changes in the LCR over time

The Society reported a Pillar 1 LCR of 187% as at 31 December 2021 (2020: 179%) which is significantly above the regulatory requirement. The LCR increased year-on-year resulting from a larger HQLA buffer marginally offset by an increase in the retail requirement.

Explanations on the actual concentration of funding sources

The Society's retail deposit base was £39.9 billion as at 31 December 2021 (2020: £37.2 billion), which represents 77.8% (2020: 78.6%) of the Society's funding (excluding capital). The Society held £11.4 billion (2020: £10.3 billion) of wholesale funding; 95% (2020: 94%) of this funding was from longer-term sources such as Covered Bonds, Medium-Term Notes, RMBS and the Bank of England funding schemes such as TFSME. The relatively large size of long-term wholesale funding deals and their typical structure as bullet maturity creates re-financing risk. As such wholesale maturities are monitored and spread to avoid concentrations.

The Society is funded predominantly by retail deposits. Funding sources include unsecured wholesale funding from financial and non-financial customers and secured wholesale funding made up of security financed transactions, covered bond issuance and asset backed security issuance.

Funding Type	Carrying amount received (£m)
Retail funding	**39,906.9**
Of which sight deposits	25,082.7
Of which term deposits not withdrawable within the following 30days	2,677.8
Wholesale funding	**11,392.8**
Unsecured wholesale funding	2,210.0
Of which loans and deposits from financial customers	1,926.8
Of which loans and deposits from non-financial customers	283.2
Secured wholesale funding	9,182.8
Of which Securities Financing Transactions	5,776.9
of which covered bond issuance	2,572.9
of which asset backed security issuance	833.0
Total Funding	**51,299.7**

Table 58 Funding sources

High-level description of the composition of the institution`s liquidity buffer

The Society's liquidity buffer is predominantly composed of the Bank of England Reserve Account with the remainder being a mix of high quality debt security assets including UK Gilts, Covered Bonds, Mortgage Back Securities and notes with Supra nationals.

Item	Value according to Article 9 (£m)
Coins and banknotes	10.3
Withdrawable central bank reserves	6,308.2
Central government assets	166.4
Multilateral development bank and international organisations assets	157.1
Extremely high quality covered bonds	125.6
Asset-backed securities (residential, CQS1)	10.3
Total Liquid Assets	**6,777.9**

Table 59 Liquidity buffer composition as at 31 December 2021

The liquidity buffer encompasses deposits with the Bank of England and holdings of highly rated and highly liquid debt securities; 96% of the liquidity portfolio is rated Aaa–Aa3 (2020: 93%). Furthermore, 97% of liquid assets are held in UK sovereign or UK financial institutions (2020: 98%).

Derivative exposures and potential collateral calls

The Society only undertakes derivative trades with counterparties where a CSA is in place. Under the terms of a CSA, the Society typically posts and receives collateral with counterparty banks (including its central clearing brokers) that offset the net mark-to-market position of derivatives with the counterparty. These arrangements are effective in mitigating the credit risk incurred in derivatives, but create a potential liquidity requirement via initial margin and variation margin calls. The Society is exposed to liquidity outflows if collateral postings are required should the Society be downgraded.

Currency mismatch in the LCR

The Society does not report in any material currency other than Sterling.

2021 Produced on a consolidated basis Currency and units (£ million)		Total unweighted value				Total weighted value			
Quarter ending on		31-Dec-21	30-Sep-21	30-Jun-21	31-Mar-21	31-Dec-21	30-Sep-21	30-Jun-21	31-Mar-21
Number of data points used in the calculation of averages		12	12	12	12	12	12	12	12
HIGH-QUALITY LIQUID ASSETS									
1	**Total high-quality liquid assets (HQLA)**					**6,884.8**	**6,679.7**	**6,360.1**	**6,085.1**
CASH OUTFLOWS									
2	Retail deposits and deposits from small business customers, of which:	**39,379,9**	**38,719.2**	**37,613.9**	**36,806.8**	**2,444.7**	**2,336.2**	**2,172.6**	**2,029.0**
3	*Stable deposits*	**16,989.1**	**16,334.0**	**15,898.0**	**16,122.0**	**849.5**	**816.7**	**794.9**	**806.1**
4	*Less stable deposits*	**12,399.8**	**11,826.6**	**10,677.1**	**9,662.7**	**1,595.2**	**1,519.5**	**1,377.7**	**1,222.9**
5	Unsecured wholesale funding	**610.3**	**606.0**	**472.1**	**390.5**	**502.8**	**502.8**	**387.1**	**321.4**
6	*Operational deposits (all counterparties) and deposits in networks of cooperative banks*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
7	*Non-operational deposits (all counterparties)*	**592.6**	**538.7**	**406.0**	**305.0**	**485.1**	**435.5**	**321.0**	**235.9**
8	*Unsecured debt*	**17.7**	**67.3**	**66.1**	**85.5**	**17.7**	**67.3**	**66.1**	**85.5**
9	Secured wholesale funding					**0.0**	**0.0**	**0.0**	**0.0**
10	Additional requirements	**269.6**	**241.3**	**243.2**	**226.6**	**269.6**	**241.3**	**243.2**	**226.6**
11	*Outflows related to derivative exposures and other collateral requirements*	**223.6**	**230.4**	**232.2**	**225.3**	**223.6**	**230.4**	**232.2**	**225.3**
12	*Outflows related to loss of funding on debt products*	**46.0**	**10.9**	**11.0**	**1.3**	**46.0**	**10.9**	**11.0**	**1.3**
13	*Credit and liquidity facilities*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
14	Other contractual funding obligations	**46.5**	**44.3**	**48.1**	**20.4**	**28.0**	**27.5**	**31.3**	**3.8**
15	Other contingent funding obligations	**2,829.3**	**2,824.6**	**2,693.1**	**2,581.6**	**720.1**	**710.4**	**668.2**	**643.8**
16	**TOTAL CASH OUTFLOWS**					**3,965.2**	**3,818.2**	**3,502.4**	**3,224.6**
CASH INFLOWS									
17	Secured lending (e.g. reverse repos)	**0.0**	**1.7**	**1.7**	**15.6**	**–**	**–**	**–**	**–**
18	Inflows from fully performing exposures	**250.5**	**253.3**	**251.1**	**248.7**	**191.0**	**195.0**	**193.7**	**192.2**
19	Other cash inflows	**8.6**	**5.7**	**5.4**	**3.8**	**8.6**	**5.7**	**5.4**	**3.8**
20	**TOTAL CASH INFLOWS**	**259.1**	**260.7**	**258.2**	**268.1**	**199.6**	**200.7**	**199.1**	**196.0**
EU-20a	*Fully exempt inflows*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
EU-20b	*Inflows Subject to 90% Cap*	**–**	**–**	**–**	**–**	**–**	**–**	**–**	**–**
EU-20c	*Inflows Subject to 75% Cap*	**259.1**	**260.7**	**258.2**	**268.1**	**199.6**	**200.7**	**199.1**	**196.0**
21	**LIQUIDITY BUFFER**					**6,884.8**	**6,679.7**	**6,360.1**	**6,085.1**
22	**TOTAL NET CASH OUTFLOWS**					**3,765.6**	**3,617.5**	**3,303.3**	**3,028.6**
23	**LIQUIDITY COVERAGE RATIO (%)**					**182.8%**	**184.6%**	**192.5%**	**200.9%**

Table 60 Quantitative information of LCR 2021

2020 Produced on a consolidated basis Currency and units (£ million)		Total unweighted value				Total weighted value			
Quarter ending on		31-Dec-20	30-Sep-20	30-Jun-20	31-Mar-20	31-Dec-20	30-Sep-20	30-Jun-20	31-Mar-20
Number of data points used in the calculation of averages		12	12	12	12	12	12	12	12
HIGH-QUALITY LIQUID ASSETS									
1	**Total high-quality liquid assets (HQLA)**					5,888.3	5,542.2	5,646.3	5,772.2
CASH OUTFLOWS									
2	Retail deposits and deposits from small business customers, of which:	36,219.0	35,840.4	35,782.9	35,554.6	1,958.6	1,912.2	1,937.8	1,898.6
3	*Stable deposits*	16,369.7	16,685.2	16,811.4	17,308.2	818.5	834.3	840.6	865.4
4	*Less stable deposits*	9,160.3	8,756.0	8,957.7	8,487.1	1,140.1	1,077.9	1,097.2	1,033.2
5	Unsecured wholesale funding	265.7	156.8	194.5	190.7	216.6	112.6	149.9	139.8
6	*Operational deposits (all counterparties) and deposits in networks of cooperative banks*	–	–	–	–	–	–	–	–
7	*Non-operational deposits (all counterparties)*	180.3	119.4	155.7	181.4	131.2	75.2	111.1	130.5
8	*Unsecured debt*	85.4	37.4	38.8	9.3	85.4	37.4	38.8	9.3
9	Secured wholesale funding					–	–	–	–
10	Additional requirements	272.4	274.0	270.5	267.5	272.4	274.0	270.5	267.5
11	*Outflows related to derivative exposures and other collateral requirements*	216.8	218.9	215.7	212.9	216.8	218.9	215.7	212.9
12	*Outflows related to loss of funding on debt products*	55.6	55.1	54.8	54.6	55.6	55.1	54.8	54.6
13	*Credit and liquidity facilities*	–	–	–	–	–	–	–	–
14	Other contractual funding obligations	27.1	28.9	26.2	24.5	11.2	11.8	8.5	9.3
15	Other contingent funding obligations	2,398.1	2,298.5	2,364.0	2,251.7	617.2	609.0	649.9	646.8
16	**TOTAL CASH OUTFLOWS**					3,076.0	2,919.6	3,016.6	2,962.0
CASH INFLOWS									
17	Secured lending (e.g. reverse repos)	15.6	13.9	13.9	–	–	–	–	–
18	Inflows from fully performing exposures	246.3	241.3	232.6	224.9	190.0	185.6	179.1	173.8
19	Other cash inflows	5.3	17.7	20.6	21.6	5.3	17.7	20.6	21.6
20	**TOTAL CASH INFLOWS**	267.2	272.9	267.1	246.5	195.3	203.3	199.7	195.4
EU-20a	*Fully exempt inflows*	–	–	–	–	–	–	–	–
EU-20b	*Inflows Subject to 90% Cap*	–	–	–	–	–	–	–	–
EU-20c	*Inflows Subject to 75% Cap*	267.2	272.9	267.1	246.5	195.3	203.3	199.7	195.4
21	**LIQUIDITY BUFFER**					5,888.3	5,542.2	5,646.3	5,772.2
22	**TOTAL NET CASH OUTFLOWS**					2,880.7	2,716.3	2,816.9	2,766.6
23	**LIQUIDITY COVERAGE RATIO (%)**					204.4%	204.0%	200.4%	208.6%

Table 61 Quantitative information of LCR 2020

Appendix 8. **Glossary**

The following glossary defines terminology within the Pillar 3 disclosures to assist the reader and to facilitate comparison with publications by other institutions:

Term	Definition
Accounts	The Society's Annual Report & Accounts
Additional Tier 1 (AT 1) capital	Capital that meets certain criteria set out in CRD IV. In particular, the criteria require that upon the occurrence of a trigger event, the AT 1 capital instrument converts to a form of Common Equity Tier 1 capital or the principal is written down on a permanent basis or on grandfathered instruments such as Permanent Interest Bearing Shares (PIBS).
Arrears	The financial value of unpaid obligations, which arise when contractual payments are not paid as they fall due.
Average loan to value	The average of individual loan to values (simple average). The average loan to value of the residential mortgage book, weighted by balance (balance weighted). For indexed loan to value – see 'Indexed loan to value'.
Basel III	The Basel Committee on Banking Supervision issued proposals for a strengthened capital regime in response to the financial crisis, which are referred to as Basel III. These standards were implemented in the European Union via CRD IV, which came into force on 1 January 2014.
Basel IV	The alternative industry name given to the Basel Committee's final implementation of its Basel III Banking Supervision reforms published in December 2017 addressing credit risk (standardised approach with floors and IRB), operational risk, and the leverage ratio. They are applicable from January 2022 and are phased in over five years.
Buy to let mortgage	A mortgage secured on a residential property that is rented out to tenants.
Capital Conservation Buffer (CCoB)	A CRD IV risk adjusted capital requirement for all banks that can be used to absorb losses whilst avoiding breaching minimum capital requirements.
Capital requirements	Amount of capital required to be held by the Group to cover the risk of losses and to protect against excessive leverage. The level is set by regulators and the firm's own assessment of its risk profile.

Capital Requirements Regulation and Capital Requirements Directive IV (CRD IV)	CRD IV is the European Union legislation (part regulation and part directive) which came into force from 1 January 2014 to implement Basel III, revising the capital requirements framework and introducing liquidity requirements, which regulators use when supervising firms.
Capital Requirements Regulations (CRR) leverage ratio	A ratio defined by the Capital Requirement Regulations (CRR) which measures Tier 1 capital as a proportion of total CRR leverage ratio exposures. These exposures are the sum of the on-balance sheet exposures, adjusted for derivatives and securities financing transaction exposures, and off-balance sheet items. These requirements are replaced by the UK leverage ratio as at 1 January 2022.
Capital resources	Capital comprising the general reserve, fair value through other comprehensive income (FVOCI) reserve, Additional Tier 1 capital less all required regulatory adjustments.
Central clearing	The process by which parties to an OTC derivative contract replace this with a separate contract with a central counterparty, which takes over each party's positions under the original contract.
Collateral	Security pledged by the borrower to the lender in case of default.
Common Equity Tier 1 (CET 1) capital	Common Equity Tier 1 capital comprises general reserves and the fair value through other comprehensive income (FVOCI) reserve, less regulatory deductions. Common Equity Tier 1 must absorb losses on a going concern basis.
Common Equity Tier 1 (CET 1) ratio	Common Equity Tier 1 capital as a percentage of risk weighted assets.
Core Capital Deferred Shares (CCDS)	A form of Common Equity Tier 1 (CET 1) capital. The Society's Perpetual Capital Securities (PCS) convert into CCDS at the rate of one CCDS for every £67 PCS held if the end-point CET 1 ratio, calculated on either an individual or consolidated basis, falls below 7%.
Countercyclical Buffer (CCyB)	A CRD IV risk adjusted capital requirement for all banks that is varied over the financial cycle to match the resilience of the banking system to the scale of risks faced.
Countercyclical Leverage Buffer (CCLB)	A leverage capital requirement under the UK leverage regime that is set at 35% of the corresponding risk adjusted Countercyclical Buffer (CCyB).
Counterparty credit risk (CCR)	Counterparty credit risk is the risk that the counterparty to a transaction could default before the final settlement of the transaction's cash flows.

Covered bonds	Debt securities that are backed by both the resources of the issuer and a portfolio of mortgages that are segregated from the issuer's other assets solely for the benefit of the holders of the covered bonds. The Society issues covered bonds as part of its funding activities.
Credit quality step	A credit quality assessment scale as set out in CRD IV.
Credit risk	The risk that borrowers or counterparties do not meet their financial obligations to the Society as they fall due. Within this class, the Society considers risks arising from retail credit risk and treasury credit risk to be individual Principal risk categories.
Credit risk mitigation	Techniques used to reduce the potential loss in the event that a customer (borrower or counterparty) becomes unable to meet its obligations. This may include the taking of financial or physical security, set off or netting.
Credit valuation adjustment	An adjustment to the valuation of financial instruments held at fair value to reflect the creditworthiness of the counterparty.
Debt securities	Transferable instruments creating or acknowledging indebtedness. They include bonds, certificates of deposit and loan notes. The holder of a debt security is typically entitled to the payment of principal and interest, together with other contractual rights under the terms of the issue. Debt securities are generally issued for a fixed term and redeemable by the issuer at the end of that term. Debt securities can be secured on other assets or unsecured.
Default	Circumstances in which the probability of default is taken as 100% for the purposes of the calculation of regulatory capital and compliance with CRD IV. This is defined as when an account reaches a pre-defined past due status or where, on accounts that are up to date or in arrears by less than the pre-defined status, certain unlikeliness to pay indicators have been met. The unlikeliness to pay indicators are those that the Society has determined as having a higher propensity to eventually reaching the pre-defined arrears status.
Deferred tax asset/(liability)	Corporation tax recoverable (or payable) in future periods as a result of the carry-forward of tax losses or unused tax credits, or from deductible (or taxable) temporary differences between the accounting value of assets and liabilities and the tax base of those assets and liabilities.
Derivative financial instrument	A contract or agreement which derives its value or cash flows from changes in an underlying index such as an interest rate, foreign exchange rate or market index. The most common type of derivative instruments are interest rate swaps.

Term	Definition
Encumbered assets	Assets used to secure liabilities or otherwise pledged. This excludes loans and advances to customers that, although technically encumbered, are held in respect of undrawn self-issued notes under the Group's covered bond and securitisation programmes.
End-point	Full implementation of regulation (for example, CRD IV) with no transitional provisions.
Enterprise Risk Management Framework (ERMF)	A Board approved framework which provides the context, guidance and principles needed for cohesive risk management activity across the Society and its subsidiaries.
European Banking Authority (EBA)	An independent European Union authority which works to ensure effective and consistent financial regulation and supervision across the European banking sector.
Expected credit loss (ECL)	The present value of all cash shortfalls over the expected life of the financial instrument. The term is used for the accounting for impairment provisions under the new IFRS 9 standard.
ECL – 12 month	Cash shortfalls resulting from default events that are possible in the next 12 months, weighted by the probability of that default occurring.
ECL – lifetime	Cash shortfalls resulting from default events that are possible over the remaining expected life of the loan, weighted by the probability of that default occurring.
Expected loss	A calculation under the IRB approach to estimate the potential losses on current exposures due to expected defaults over a 12 month time period.
Exposure	The quantified potential for loss that might occur as a result of a risk occurring.
Exposure at Default (EAD)	A parameter used in IRB approaches and under IFRS 9 to estimate the amount outstanding at the time of default.
External Credit Assessment Institution (ECAI)	An ECAI (e.g. Moody's, Standard and Poor's and Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
Fair value	The price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date in the principal or, in its absence, the most advantageous market to which the Group has access at that date.

Fair value through other comprehensive income (FVOCI) reserve	Financial assets held at fair value on the Balance Sheet with changes on the fair value recognised through other comprehensive income.
Financial Conduct Authority (FCA)	A statutory body responsible for the conduct of business regulation and supervision of UK financial institutions in the UK.
Financial Policy Committee (FPC)	A committee based at the Bank of England, charged with identifying, monitoring and taking action to reduce or remove systemic risks with a view to protect and enhance the resilience of the UK financial system. It is also responsible for supporting the economic policy of the UK Government.
Fitch	A credit rating agency which provides credit ratings and research covering financial institutions and governments and their debt instruments and securities.
Forbearance	Forbearance takes place when a concession, which can be temporary or permanent, is made on the contractual terms of a loan in response to the borrower's financial difficulties.
General reserve	The general reserve is the accumulation of historical and current year profits and includes remeasurements of the defined benefit pension plan and distributions to holders of Perpetual Capital Securities (net of tax).
Gilts/Government investment securities (gilts)	The name given to long-term fixed income debt securities (bonds) issued by the UK Government.
IFRS/IAS	International Financial Reporting Standards/International Accounting Standards. A set of international accounting standards stating how particular types of transactions and other disclosures should be reported in financial statements.
Impaired loans	Impaired loans are defined as those which are defaulted loans in IFRS 9 stage 3.
Impairment provision	Expected Credit Losses (ECL) held under IFRS 9 – see ECL glossary definition.
Indexed loan to value	Loan to value calculated on the basis of the latest property valuation being adjusted by the relevant House Price Index movement since that date.
Interest rate swap	A contract under which two counterparties agree to exchange periodic interest payments based on a predetermined notional principal amount.

Internal Capital Adequacy Assessment Process (ICAAP)	The Society's own assessment of the amount of capital that it needs to hold to support all relevant current and future risks. This assessment includes determination of a number of capital buffers to be held in case of potential future economic stress, and provides confirmation that the Society has appropriate processes in place to ensure compliance with regulatory requirements.
Internal Liquidity Adequacy Assessment Process (ILAAP)	The Society's own assessment of the liquidity resources that are required to remain within the risk tolerances it has set. This will include an evaluation of potential stresses based on regulatory benchmarks and on Society-specific tests.
Internal Ratings-Based (IRB) approach	An advanced approach to measuring capital requirements in respect of credit risk under Pillar 1. The IRB approach may only be used with permission from the PRA.
ISDA	International Swaps and Derivatives Association is the global trade association for over-the-counter (OTC) derivatives and providers of the industry-standard documentation for derivative transactions.
Leverage ratio	A calculation brought in as part of CRD IV which measures the relationship between eligible Tier 1 capital and exposures to on and off-balance sheet items. There are two bases of calculation – see Capital Requirements Regulations (CRR) leverage ratio and UK leverage ratio.
Liquidity Coverage Ratio (LCR)	A measure brought in as part of CRD IV which aims to ensure that an entity maintains an adequate level of liquidity to meet its needs for a 30 day period under severe stress conditions.
Limited Liability Partnership (LLP)	A partnership in which some or all partners have limited liabilities.
Loan to value (LTV)	The amount of mortgage loan as a percentage of the value of the property.
Loss Given Default (LGD)	A parameter used under IRB approaches and IFRS 9 to estimate the difference between exposure at default (EAD) and the net amount of the expected recovery expressed as a percentage of EAD.
Member	A person who holds a share in the Society or has a mortgage loan with the Society.
Minimum requirement for own funds and eligible liabilities (MREL)	A requirement under the Bank Recovery and Resolution Directive (BRRD) which requires deposit takers to hold minimum levels of capital plus debt eligible for bail-in.
Moody's	Moody's Investor Services is a credit rating agency which provides credit ratings and research covering financial institutions and governments and their debt instruments and securities.
Mortgage backed securities	Asset backed securities that represent interests in a group of mortgages which give the investor the right to cash received from future mortgage payments of both principal and interest.

Near-prime	Loans to borrowers with marginally weakened credit histories such that their credit risk is greater than 'prime' customers, but is not considered heavily adverse.
Netting	The ability to reduce credit risk exposures through entering into ISDA master netting agreements (whereby outstanding transactions with the same party can be settled net following a default or other predetermined event) and the receipt of financial collateral.
Over-the-counter (OTC)	Contracts that are traded (and privately negotiated) directly between two parties without going through an exchange or other intermediary. They offer flexibility because, unlike standardised exchange-traded products, they can be tailored to fit specific needs.
Owner-occupier mortgage	A mortgage on residential property that is to be occupied by the borrower.
Past due	A financial asset such as a loan is past due when the counterparty has failed to make a payment when contractually due.
Permanent Interest Bearing Shares (PIBS)	Unsecured, perpetual deferred shares of the Society offering a fixed coupon. PIBS rank equally with each other and Perpetual Capital Securities. They rank behind all other creditors of the Society including subordinated liabilities and the claims of Shareholding Members (other than Perpetual Capital Securities) as to principal and interest. Under Basel III PIBS are included as Tier 1 under transitional rules only.
Perpetual Capital Securities (PCS)	Securities that pay a non-cumulative coupon at the discretion of the Society. They rank equally with each other and Permanent Interest Bearing Shares (also AT 1 capital) but behind all other creditors of the Society, including subordinated liabilities and the claims of Shareholding Members (other than Permanent Interest Bearing Shares), as to principal and interest.
Pillar 1	The part of the Basel Framework which sets out the regulatory minimum capital requirements for credit, market and operational risk.
Pillar 2	The part of the Basel Framework which sets out the processes by which financial institutions review their overall capital adequacy. Supervisors then evaluate how well financial institutions are assessing their risks and take appropriate actions in response to the assessments. This includes all risks (including Pillar 1 risks) – TCR (see below) is an outcome of Pillar 2.
Pillar 3	The part of the Basel Framework which sets out the disclosure requirements for firms to publish details of their risks, capital and risk management. The aims are greater transparency and strengthening market discipline.
Point-in-Time (PiT)	A modelling approach which assesses the credit risk of an exposure at a single point in time.
Post model adjustment (PMA)	A PMA is applied when the Society considers that a modelled output is not sufficiently accurate or complete due to there being

	potential for additional risks that have not been identified or that cannot be adequately modelled.
Principal risk	Principal risk is a class of significant inherent risk which could materially compromise the Society's ability to grow and provide attractive products to savings and borrowing members.
Probability of Default (PD)	An estimate of the probability that a borrower will default on their credit obligations over a fixed time period. With respect to impairment provisions under IFRS 9, 12 month ECLs use 12 month PDs, whilst a lifetime ECL uses the estimated PD over the remaining contractual life of the loan. With respect to IRB, PD is the probability of a loan defaulting in the next 12 months calculated as an average over an economic cycle.
Prudential Regulation Authority (PRA)	The statutory body responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers and major investment firms. The PRA is a subsidiary of the Bank of England.
Residential Mortgage Backed Securities (RMBS)	Securities issued with interest and principal backed by a group of residential mortgages which give the investor the right to cash received from future mortgage payments of both principal and interest.
Residual maturity	The remaining period to the contractual maturity date of a financial asset or financial liability.
Resolution Authority	In the UK, the Resolution Authority is the Bank of England who is responsible for taking charge, recapitalising and restructuring a firm, on account of the firms realised or expected failure.
Reverse stress test	Regulatory stress test that requires a firm to assess scenarios and circumstances that would render its business model unviable, thereby identifying potential business vulnerabilities.
Risk appetite	The articulation of the level of risk that the Society is willing to accept in order to safeguard the interests of the Society's members, whilst also achieving business objectives.
Risk weighted assets (RWAs)	The value of assets, after adjustment, to reflect the degree of risk they represent in accordance with the relevant capital rules.
Sale and repurchase agreement (repo)	An agreement to sell a financial security together with a commitment by the seller to repurchase the asset at a specified price on a given date. In substance this forms a secured loan, with the difference between the purchase price and repurchase price being the interest rate.
Securitisation	A pool of loans used to back the issuance of new securities. The loans are transferred to a structured entity which then issues securities (RMBS) backed by the assets. The Group has used residential mortgages as the loan pool for securitisation purposes.
Self-certified mortgage	An owner-occupier mortgage where the lending decision with respect to affordability has been based solely on the borrower's declaration of their income.

Significant increase in credit risk (SICR)	A significant increase in credit risk on a financial asset is judged to have occurred when an assessment, using quantitative and qualitative factors, identifies at a reporting date that the credit risk has increased significantly since the asset was originally recognised.
Stage 1	Stage 1 assets are assets which have not experienced a significant increase in credit risk since the asset was originally recognised on the Balance Sheet. 12 month ECLs are recognised as the impairment provision for all financial assets on initial recognition. Interest revenue is the EIR on the gross carrying amount.
Stage 2	Stage 2 assets have experienced a significant increase in credit risk since initial recognition. Lifetime ECL is recognised as an impairment provision. Interest revenue is EIR on the gross carrying amount.
Stage 3	Stage 3 assets are identified as in default and considered credit impaired. Lifetime ECL is also recognised as an impairment provision. Interest revenue is the EIR on the net carrying amount.
Standardised approach	The basic method used to calculate capital requirements for credit and operational risk. In this approach the risk weighting used in the capital calculation is determined by specified percentages.
Stress testing	Testing undertaken to provide an understanding of the Society's resilience to internal and external shocks.
Structured entity	An entity in which voting or similar rights are not the dominant factor in deciding control. Structured entities are consolidated when the substance of the relationship indicates control.
Subordinated debt	A form of Tier 2 capital that is unsecured. Subordinated notes rank equally with each other and behind all other creditors of the Society and the claims of Shareholding Members (other than holders of Permanent Interest Bearing Shares and Perpetual Capital Securities) as to principal and interest. Under Basel III, they are included as Tier 2 under transitional rules only.
Subscribed capital	See Permanent Interest Bearing Shares.

Supervisory Review and Evaluation Process (SREP)	The PRA assessment of a firm's own Individual Capital Assessment (ICA) under Pillar 2.
Supplementary Leverage Ratio Buffer (SLRB)	Applied to systemically important banks and building societies. As a guiding principle, the FPC sets the buffer at 35% of the risk weighted Systemic Risk Buffer.
Systemic Risk Buffer (SRB)	Buffer set for ring-fenced banks and large building societies to reduce their probability of failure or distress commensurately with the greater cost their failure or distress would have for the UK economy.
Term Funding Scheme and the Term Funding Scheme with additional incentives for SMEs	The Term Funding Scheme (TFS) and the Term Funding Scheme with additional incentives for SMEs (TFSME) are tools of the Monetary Policy Committee designed to reinforce the transmission of Bank of England Base Rate cuts to those interest rates actually faced by households and businesses by providing term funding to banks and building societies at rates close to Bank of England Base Rate.
Tier 1 capital	A component of regulatory capital comprising Common Equity Tier 1 and Additional Tier 1 capital.
Tier 2 capital	A component of regulatory capital comprising qualifying subordinated debt and eligible collective impairment allowances.
Total Capital Requirement (TCR)	The minimum amount of capital the Society should hold as set by the PRA under Pillar 1 and Pillar 2A and informed by the Internal Capital Adequacy Assessment Process (ICAAP).
Trading book	A regulatory classification consisting of positions in financial instruments or commodities held by a bank with an intention to trade. The Society does not have a trading book.
The Standardised Approach: operational risk	The standardised approach to operational risk, calculated using three year historical net income multiplied by a percentage factor depending on the underlying business being considered.
UK Finance	A trade association that incorporates residential mortgage lending.
UK leverage ratio	A ratio prescribed by the PRA based on the CRR leverage ratio but modified to restrict the amount of AT 1 capital that can be included in Tier 1 capital and to exclude eligible central bank holdings from leverage ratio exposures.
Unencumbered assets	Assets readily available as collateral to secure funding. This includes loans and advances to customers that, although technically encumbered, are held in respect of undrawn self-issued notes under the Group's covered bond and securitisation programmes and are therefore readily available as collateral to secure funding or to pledge as collateral against margin calls.

Coventry Building Society is authorised by the Prudential Regulation Authority and regulated by the Financial Conduct Authority (www.fca.org.uk) and the Prudential Regulation Authority (firm reference number 150892).

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