The Cumberland

Pillar 3 Disclosures

31 March 2022

Final dated 01 June 2022

Contents

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1 Overview

1.1 Introduction

This document presents the Pillar 3 disclosures on capital and risk management of the regulated group (the Group) for the year ended 31 March 2022.

The disclosure requirements in this document apply to Cumberland Building Society and its subsidiary, Borderway Finance Limited.

1.2 Regulatory Framework for Disclosures

The Basel framework is structured around three pillars which govern minimum capital requirements, outline the supervisory review framework, and promote market discipline through disclosure requirements.

- **Pillar 1** sets out the minimum capital requirement that firms are required to meet for Credit, Market and Operational Risk.

- **Pillar 2** supervisory review process requires firms and supervisors to form a view on whether a firm should hold additional capital against risks not taken into account or not fully covered in Pillar 1 (e.g. interest rate risk in the banking book and pension obligation risk) and factors external to the firm (e.g. economic cycle effects).To comply, institutions are required to develop adequate arrangements, strategies, processes and mechanisms to maintain sound management and coverage of their risks, including maintenance of the prescribed capital.

- **Pillar 3** aims to complement the capital requirement and supervisory review process by encouraging market discipline through developing a set of disclosure requirements under the Capital Requirements Regulation (CRR) that allow market participants to assess the scope of application, risk exposures, risk assessment process and capital adequacy of firms. The Pillar 3 disclosures contained within this document have two principal purposes:

    - To meet the regulatory disclosure requirements under the Disclosure (CRR) Part of the PRA Rulebook (CRR) Instrument 2021, supplemented by any specific additional requirements of the Prudential Regulatory Authority (PRA); and

    - To provide transparency and further useful information on the capital and risk profile of the Group.

1.3 Basis of preparation

The group meets the criteria for being a 'small and non-complex' institution as introduced in the CRR II and incorporated into the PRA Rulebook under Article 433b.

The Group's policy is to comply with all requirements of the derogation for small and non-complex institutions as per article 433b of the PRA Rulebook.

These disclosures have therefore been prepared applying the concept of derogation for small and non-complex institutions.

There are no current or foreseen material practical or legal impediments to the transfer of own funds or repayment of liabilities among the parent undertaking and its subsidiaries. All figures in tables are in thousands of pounds, unless stated otherwise.

The Group's financial statements have been prepared under the historical cost convention, modified to include certain items at fair value, and in accordance with Financial Reporting Standard 102 (FRS 102) and International Accounting Standard 39 (IAS 39).

Row numbers in the below tables relate to the Prudential Regulation Authority (PRA) prescribed references within the standardised templates; where rows contain a nil value, these have been excluded in some circumstances for the purposes of enhancing the readability and understandability of these disclosures.

Disclosures have not been duplicated where items are available in the annual report.

1.4 Frequency of disclosure

Pillar 3 disclosures are prepared annually to 31 March and are published on the Society's website at the same time as the Annual Report and Accounts in accordance with Article 433 of the CRR.

1.5 Regulation changes

The CRR and Capital Requirements Directive (CRD) amendments were published in the Official Journal of the European Union on 7 June 2019, including amendments due in June 2021. However, in a joint statement, published on 16 November 2020, Her Majesty's Treasury, the PRA, and the Financial Conduct Authority (FCA) confirmed a date of 1 January 2022 for implementing those Basel III reforms which make up the UK equivalent to the outstanding elements of the EU's 2nd CRR.

The Group of Central Bank Governors and Heads of Supervision (GHOS), announced in March 2020 that the implementation of the Basel 3.1 standards would be delayed by one year to 1 January 2023. Since the year end, the PRA have confirmed that the current intention is to consult on a proposal that these changes will become effective on 1 January 2025. Throughout this document, the original and amended regulation (CRR and CRR2) and directive (CRD IV and CRD V) are collectively referred to as CRR and CRD.

Following the UK's withdrawal from the EU and the ending of the transition period, any reference to EU regulations and directives (including regulatory and implementing technical standards) should be read as a reference to the UK's version of such regulation or directive, as onshored into UK law under the European Union (Withdrawal) Act 2018, as amended by Statutory Instruments, PRA Rulebook (CRR) Instrument 2021 and PRA Rulebook: CRR Leverage Instrument 2021.

1.6 Verification

The disclosures presented within this document are subject to the same level of internal verification as that applicable to the management report included in the institutions' financial statement disclosures.

Where appropriate the Pillar 3 disclosures are reconciled to and conform with the externally audited information in the Annual Financial Statements.

The information is prepared and checked by line 1 with oversight and challenge by lines 2 and 3 as appropriate.

The Pillar 3 Disclosures document is reviewed by the Audit Committee for onward recommendation and approved by the Board alongside the Annual Report and Accounts.

1.6 Summary of key disclosures

The table below provides an overview of the Group's prudential regulatory metrics.

Table 1: UK M1 - Key Metrics

		2022 £'000	2021 £'000
	Available own funds (amounts)		
1	Common Equity Tier 1 (CET1) capital	202,581	196,664
2	Tier 1 capital	202,581	196,664
3	Total capital	202,581	198,413
	Risk-weighted exposure amounts		
4	Total risk-weighted exposure amount	994,651	965,536
	Capital ratios (as a percentage of risk-weighted exposure amount)		
5	Common Equity Tier 1 ratio (%)	20.37%	20.37%
6	Tier 1 ratio (%)	20.37%	20.37%
7	Total capital ratio (%)	20.37%	20.55%
	Additional own funds requirements based on SREP (as a percentage of risk-weighted exposure amount)		
UK 7a	Additional CET1 SREP requirements (%)	1.51%	3.14%
UK 7b	Additional AT1 SREP requirements (%)	-	-
UK 7c	Additional T2 SREP requirements (%)	-	-
UK 7d	Total SREP own funds requirements (%)	9.51%	11.14%
	Combined buffer requirement (as a percentage of risk-weighted exposure amount)		
8	Capital conservation buffer (%)	2.50%	2.50%
9	Institution specific countercyclical capital buffer (%)	-	-
UK 9a	Systemic risk buffer (%)	-	-
11	Combined buffer requirement (%)	2.50%	2.50%
UK 11a	Overall capital requirements (%)	12.01%	13.64%
12	CET1 available after meeting the total SREP own funds requirements (%)	10.86%	9.23%
	Leverage ratio		
13	Leverage ratio total exposure measure	2,407,988[1]	2,730,454
14	Leverage ratio	8.41%[1]	7.20%
	Liquidity Coverage Ratio		
15	Total high-quality liquid assets (HQLA) (Weighted value -average)	538,404[2]	438,301
UK 16a	Cash outflows - Total weighted value	230,194	205,867
UK 16b	Cash inflows - Total weighted value	29,157	20,524
16	Total net cash outflows (adjusted value)	201,037	185,343
17	Liquidity coverage ratio (%)	268%	236%
	Net Stable Funding Ratio		
18	Total available stable funding	2,718,975[3]	2,449,807
19	Total required stable funding	1,746,761	1,703,456
20	NSFR ratio (%)	156%	144%

[1] After exclusion of qualifying central bank exposure.

[2] The LCR is higher in 2022 because of higher liquidity and HQLA which increased primarily as a result of drawing additional funds from the Bank of England (TFSME) which rose from £130m (of TFS) in 2021 to £220m (of TFSME) in 2022.

[3] The NSFR is higher in 2022 because of higher available stable funding from TFSME.

1.7 Overview of Risk Weighted Exposure Amounts (RWEAs)

The RWEAs and credit risk exposures related to the standardised model for the Group are as below.

Table 2: UK OV1 - Overview of risk weighted exposure amounts

		Risk weighted exposure amounts (RWEAs)	Risk weighted exposure amounts (RWEAs)	**Total own funds requirements**
		2022	2021	**2022**
		£'000	£'000	**£'000**
1	**Credit risk (excluding CCR)**	**897,027**	**877,424**	**71,762**
2	Of which the standardised approach	897,027	877,424	71,762
3	Of which the foundation IRB (FIRB) approach	-	-	-
4	Of which slotting approach	-	-	-
UK 4a	Of which equities under the simple risk weighted approach	-	-	-
5	Of which the advanced IRB (AIRB) approach	-	-	-
6	**Counterparty credit risk - CCR**	**12,051**	**5,483**	**964**
7	Of which the standardised approach	12,051[4]	5,483	964
8	Of which internal model method (IMM)	-	-	-
UK 8a	Of which exposures to a CCP	-	239	-
UK 8b	Of which credit valuation adjustment - CVA	11,351[5]	2,189	908
9	Of which other CCR	-	-	-
15	Settlement risk	-	-	-
UK 22a	**Large exposures**	**-**	-	-
23	**Operational risk**	**85,573**	**82,629**	**6,846**
UK 23a	Of which basic indicator approach	85,573	82,629	6,846
UK 23b	Of which standardised approach	-	-	-
UK 23c	Of which advanced measurement approach	-	-	-
24	Amounts below the thresholds for deduction (subject to 250% risk weight) (For information)	5,285	8,552	423
29	**Total**	**994,651**	**965,536**	**79,572**

[4] This exposure value is inclusive of derivative counterparty and CVA RWAs.

[5] The CVA exposure value has increased in 2022 because of the increase in the positive fair value of derivative contracts in the period.

Standardised approach – Credit risk exposure and CRM effects

Standardised exposures in the table below are stated on two different bases (pre-CCF (credit conversion factor) and CRM (credit risk mitigation) and post-CCF and CRM). Note, the exposures are also net of credit risk adjustment exposures.

Table 3: UK CRM – Standardised approach – Credit risk exposure and CRM effects 2022

Exposure classes	Exposures before CCF and before CRM		Exposures post CCF and post CRM		RWAs and RWAs density	
	On-balance-sheet exposures	Off-balance-sheet exposures	On-balance-sheet exposures	Off-balance-sheet amount	RWAs	RWAs density (%)[6]
	£'000	£'000	£'000	£'000	£'000	
Central governments or central banks	502,793	-	502,793	-	-	0.0%
Regional government or local authorities	-	-	-	-	-	0.0%
Public sector entities	-	-	-	-	-	0.0%
Multilateral development banks	15,218	-	15,218	-	-	0.0%
International organisations	-	-	-	-	-	0.0%
Institutions	48,574	-	48,574	-	11,218	23.1%
Corporates	-	-	-	-	-	0.0%
Retail	22,820	8,868	22,596	84	17,010	75.0%
Secured by mortgages on immovable property	2,232,965	128,153	2,231,014	25,630	828,724	36.7%
Exposures in default	6,860	-	6,291	-	6,291	100.0%
Exposures associated with particularly high risk	574	-	574	-	862	150.0%
Covered bonds	29,789	-	29,789	-	3,779	12.7%
Institutions and corporates with a short-term credit assessment	-	-	-	-	-	0.0%
Collective investment undertakings	-	-	-	-	-	0.0%
Equity	6,717	-	6,717	-	6,717	100.0%
Other items	21,721	-	19,257	-	22,426	116.5%
TOTAL	**2,888,031**	**137,021**	**2,882,823**	**25,714**	**897,027**	**30.8%**

[6] RWA density is RWA expressed as a percentage of exposures post CCF and CRM.

Table 4: UK CRM – Standardised approach – Credit risk exposure and CRM effects 2021

Exposure classes	Exposures before CCF and before CRM		Exposures post CCF and post CRM		RWAs and RWAs density	
	On-balance-sheet exposures	Off-balance-sheet exposures	On-balance-sheet exposures	Off-balance-sheet amount	RWAs	RWAs density (%)
	£'000	£'000	£'000	£'000	£'000	
Central governments or central banks	437,449	-	437,449	-	-	0.0%
Regional government or local authorities	-	-	-	-	-	0.0%
Public sector entities	-	-	-	-	-	0.0%
Multilateral development banks	-	-	-	-	-	0.0%
International organisations	-	-	-	-	-	0.0%
Institutions	33,724	-	33,724	-	8,620	25.6%
Corporates	-	-	-	-	-	0.0%
Retail	21,573	9,382	21,563	110	16,334	75.4%
Secured by mortgages on immovable property	2,157,012	90,425	2,154,262	18,085	803,809	37.0%
Exposures in default	16,507	-	16,057	-	16,698	104.0%
Exposures associated with particularly high risk	970	-	970	-	1,454	150.0%
Covered bonds	7,082	-	7,082	-	708	10.0%
Institutions and corporates with a short-term credit assessment	-	-	-	-	-	0.0%
Collective investment undertakings	-	-	-	-	-	0.0%
Equity	5,824	-	5,824	-	5,824	100.0%
Other items	23,977	-	23,977	-	23,977	100.0%
TOTAL	**2,704,118**	**99,807**	**2,700,908**	**18,195**	**877,424**	**32.3%**

Standardised approach – exposures by asset class

Exposures in the table below are presented on a post CRM (Credit Risk Mitigation) and post CCF (Credit Conversion Factor) basis applied in accordance with Part Three, Title II, Chapter 4 of the CRR.

The Group makes limited use of External Credit Assessment Institutions (ECAIs) assessments for its Standardised exposures. Where a credit assessment is used this must be provided by an eligible ECAI from the PRA's approved list. The appropriate risk weight to apply to the credit risk exposure is determined by assigning the exposure to the relevant credit quality step under CRD V, based on the PRA's mapping of credit assessments to credit quality steps.

For the below disclosure, exposures are classed as 'rated' only where an ECAI rating has been used to derive the risk weight. Where a rating is unavailable, or where the risk weight has been determined by application of specific CRR provisions, exposures have been classed as 'unrated'. This also applies to central governments or central banks exposures within the UK and EEA that receive a zero per cent risk weight in line with regulatory permission.

Table 5: CR5 - Standardised approach - exposure by asset class 2022

2022

	Exposure classes (£'000)	Risk weight											Total	Of which unrated
		0%	4%	10%	20%	35%	50%	75%	100%	150%	250%	Others		
1	Central governments or central banks	502,793	-	-	-	-	-	-	-	-	-	-	502,793	502,793
2	Regional government or local authorities	-	-	-	-	-	-	-	-	-	-	-	-	-
3	Public sector entities	-	-	-	-	-	-	-	-	-	-	-	-	-
4	Multilateral development banks	15,218	-	-	-	-	-	-	-	-	-	-	15,218	-
5	International organisations	-	-	-	-	-	-	-	-	-	-	-	-	-
6	Institutions	-	-	-	43,565	-	5,009	-	-	-	-	-	48,574	27,813
7	Corporates	-	-	-	-	-	-	-	-	-	-	-	-	-
8	Retail exposures	-	-	-	-	-	-	22,680	-	-	-	-	22,680	22,680
9	Exposures secured by mortgages on immovable property	-	-	-	-	2,081,050	-	11,020	164,574	-	-	-	2,256,644	2,256,644
10	Exposures in default	-	-	-	-	-	-	-	6,291	-	-	-	6,291	6,291
11	Exposures associated with particularly high risk	-	-	-	-	-	-	-	-	574	-	-	574	574
12	Covered bonds	-	-	21,784	8,005	-	-	-	-	-	-	-	29,789	-
13	Exposures to institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-	-	-	-	-	-
14	Units or shares in collective investment undertakings	-	-	-	-	-	-	-	-	-	-	-	-	-
15	Equity exposures	-	-	-	-	-	-	-	6,717	-	-	-	6,717	-
16	Other items	-	-	-	-	-	-	-	17,143	-	2,114	-	19,257	19,257
17	**TOTAL**	**518,011**	**-**	**21,784**	**51,570**	**2,081,050**	**5,009**	**33,700**	**194,725**	**574**	**2,114**	**-**	**2,908,537**	**2,836,052**

Table 6: CR5 - Standardised approach - exposure by asset class 2021

2021

	Exposure classes (£'000)	Risk weight											Total	Of which unrated
		0%	4%	10%	20%	35%	50%	75%	100%	150%	250%	Others		
1	Central governments or central banks	437,449	-	-	-	-	-	-	-	-	-	-	437,449	437,449
2	Regional government or local authorities	-	-	-	-	-	-	-	-	-	-	-	-	-
3	Public sector entities	-	-	-	-	-	-	-	-	-	-	-	-	-
4	Multilateral development banks	-	-	-	-	-	-	-	-	-	-	-	-	-
5	International organisations	-	-	-	-	-	-	-	-	-	-	-	-	-
6	Institutions	-	-	-	27,683	-	6,041	-	-	-	-	-	33,724	8,006
7	Corporates	-	-	-	-	-	-	-	-	-	-	-	-	
8	Retail exposures	-	-	-	-	-	-	21,673	-	-	-	-	21,673	21,673
9	Exposures secured by mortgages on immovable property	-	-	-	-	1,998,254	-	14,362	159,731	-	-	-	2,172,347	2,172,347
10	Exposures in default	-	-	-	-	-	-	-	14,776	1,281	-	-	16,057	16,057
11	Exposures associated with particularly high risk	-	-	-	-	-	-	-	-	970	-	-	970	970
12	Covered bonds	-	-	7,082	-	-	-	-	-	-	-	-	7,082	-
13	Exposures to institutions and corporates with a short-term credit assessment	-	-	-	-	-	-	-	-	-	-	-	-	-
14	Units or shares in collective investment undertakings	-	-	-	-	-	-	-	-	-	-	-	-	-
15	Equity exposures	-	-	-	-	-	-	-	5,824	-	-	-	5,824	-
16	Other items	-	-	-	-	-	-	-	23,977	-	-	-	23,977	23,977
17	**TOTAL**	**437,449**	**-**	**7,082**	**27,683**	**1,998,254**	**6,041**	**36,035**	**204,308**	**2,251**	**-**	**-**	**2,719,103**	**2,680,479**

2 Risk Management Approach

2.1 Risk Statement

The Cumberland's overall Risk Appetite is as follows:

The Cumberland will only pursue a strategy that drives towards its vision, is consistent with the Society's values and does not exceed stated risk appetite and minimum required standards.

The Cumberland is a prudent business that ensures compliance with all applicable laws and regulations and maintains a robust control environment delivered through a consistently applied Risk Management Framework (RMF).

The chosen strategy must be resilient enough to withstand severe but plausible stresses and allow the business to recover and minimise the detrimental impacts from unforeseen shocks.

The Risk Appetite is managed through a comprehensive Risk Appetite Framework and is reported to every Board Risk Committee (BRC) with a summarised view presented to Board in the months when the BRC does not sit. All the agreed measures are owned by individual members of the Senior Leadership Team (SLT) with limits and triggers agreed by Board.

The Society has elected to omit disclosing key ratios and figures relating to its risk appetite, as they are proprietary information as per CRR Article 432.

2.2 Declaration

In accordance with the requirements of CRR Article 435I, the Society's Board are satisfied that the risk arrangements in place at the Society are adequate with regard to the Society's profile and strategy.

2.3 Strategies and Processes to Manage Risks

2.3.1 Risk Management Framework

The Society applies a consistent approach to Risk Management through its RMF.

The Society uses the best practice three lines of Defence approach, ensuring that risks are managed in the areas they are best understood (i.e., the business). A second line of defence risk team ensures consistency through the use of frameworks, tools and policies and provides independent oversight to the Board through risk reporting and the outputs and findings from the combined assurance plan. The third line of defence, the internal audit function, provides independent assurance over all elements of the Society and helps ensure appropriate risk capabilities and approaches.

The three lines of defence model is summarised in the following table:

Table 7: Three lines of defence model

1st Line (Line Management)	2nd Line (Risk Management)	3rd Line (Internal Audit)
• Ownership of day-to-day risk management. • Compliance with relevant regulation and legislation. • Identifies, manages, monitors, and mitigates risks faced by the Society. • Defines and operates operational controls and limits. (Not Board limits.) • Assesses key risk indicators and market conditions. • Produces management information and reports on risks.	• Design and development of the overall risk management framework and associated policies. • Oversight, monitoring and reporting of significant risks. • Oversight, monitoring and reporting against risk appetite. • Oversight of the Society's Customer Outcome Testing Framework. • Monitor business as usual adherence to framework. • Monitor and report on regulatory compliance. • Report independently to Board through BRC	• Internal Audit sits as an independent and objective assurance function designed to add value and improve the Society's operations by helping it accomplish its objectives by bringing a systematic, disciplined approach to evaluate and improve the effectiveness of risk management, control, and governance processes. • Internal Audit reports independently to the Board through the Board Audit Committee • Internal Audit sits as the Society's third line of defence and, therefore, the department has no operational responsibilities. This helps enforce the independence of the Internal Audit Function.

Where considered necessary, the Group uses external specialists to support its Risk and Internal Audit functions through 'co-sourcing' in specific areas.

The Key Risk Frameworks component of the RMF details how risk influences and is part of the overall strategy development cycle for the Society.

A policy Framework is in place that determines the approach for setting minimum standards, with a Strategic Risk Policy detailing the minimum requirements for strategy setting and strategic considerations. This is complemented by a Risk Appetite Framework that determines the risk limits set by Board to act as guiderails under which the SLT can deliver the strategy in a sustainable manner consistent with the values and working towards the overall vision and purpose.

2.3.2 Strategies and processes to manage risks for each category of risk

2.3.2.1 Credit Risk

The Society is primarily exposed to credit risk in respect of mortgage customers or Treasury counterparties being unable to meet their obligations as they become due. Credit risk also arises in the operations of Borderway Finance Limited, the Group's vehicle finance business, and in relation to current account overdrafts.

2.3.2.2 Loans fully secured on residential property

The Credit Risk Policy, Lending Criteria and Lending Limits document the Society's approach to and appetite for residential lending credit risk. Policy is reviewed annually, or on a more frequent basis if there are changes to the operating environment. Lending Criteria are updated more frequently and are approved through the Credit Risk and Board Risk Committees (as required). Lending mandates are strictly controlled, and applications, where criteria dictate, are reviewed by a specialist residential mortgage underwriting team. Applications outside the highest level in individual mandate are considered by the Credit Risk Committee.

The Society's principal focus in lending secured on residential property, is on owner occupier lending via its branch network, Telephony and National Lending Teams on a direct basis. In addition, the Society has accepted introduced residential mortgage business, historically this has been almost all located outside of the branch operating area, from a small number of brokers, but as part of our growth strategy this has now been extended to include a similarly small number of brokers in our operating area.

As a result of its long-established approach, the Society's owner occupier residential lending exhibits a strong concentration within its branch operating area of Cumbria, Dumfries & Galloway, north Lancashire, and west Northumberland. This is monitored by the BRC each quarter, with a detailed assessment being produced on an annual basis and included as an appendix in the Society's ICAAP. Research has shown that customers value the 'local' nature of the Society and its branch network, and the Society's detailed knowledge of its operating area, when combined with its direct approach to residential lending, is regarded as a strength in ensuring the quality of its lending. This is strongly reflected in the Society's favourable arrears performance (both pre and post COVID) when compared with national statistics. Overall, the Society regards this concentration in a positive manner, as a focus and a demonstration of the strength of its regional franchise.

The Society increased its lending in the Holiday Let and Buy to let markets during the years prior to COVID and saw strong performance in the Holiday Let book post the removal of COVID restrictions, which when combined with the emerging performance of the introduced business channel, has reduced the geographical concentration within its mortgage book. Buy to let and Holiday let lending to corporate bodies and professional landlords is managed by the specialist Cumberland Commercial team. All Buy to Let and Holiday Let lending is restricted to a maximum loan to value ratio of 75%.

2.3.2.3 Loans fully secured on land

The Credit Risk Policy, Lending Criteria and Lending Limits document the Society's approach to, and appetite for, commercial lending credit risk, covering as well as loans fully secured on land, Holiday and Buy to Let lending managed by the Cumberland Commercial team.

Policy is reviewed annually, or on a more frequent basis if there are changes to the operating environment. Lending Criteria are updated more frequently and are approved through Credit Risk and Board Risk Committees (as required). The Society's specialist commercial lending managers produce detailed appraisals of each application, and all applications are considered by either a specialist Commercial Underwriter or the Credit Risk Committee. Whilst there is currently a concentration of commercial lending within the Society's branch operating area, principally with respect to tourism in the Lake District, this is less pronounced than for owner occupier residential lending and is anticipated to change further in line with the Society's growth strategy in respect of Commercial Business; the Board continues to monitor the geographical and sectoral compositions of the loan book that is fully secured on land.

2.3.2.4 Treasury

The Assets & Liabilities Committee (ALCO) is responsible for recommending credit limits on Treasury counterparties for approval by the Board, and these are set out in the Financial Risk Management Policy (FRMP) and reviewed annually or more frequently if appropriate. The list of counterparties consists of those which, on first inclusion, meet or exceed minimum credit rating agency rating; exposure limits are reconsidered following any change to the counterparty's credit rating. Credit exposure limits for building societies (rated and unrated) are reviewed annually following receipt of annual results. Information on rated counterparties is reviewed in detail by the Committee when it believes that this is appropriate. The permitted credit limit for counterparties includes where appropriate exposure in respect of the replacement cost of derivative financial instruments.

3.2 Financial Risk

3.2.1 Interest Rate Risk in the Banking Book (IRRBB)

IRRBB reflects the current or prospective risk to both the earnings and economic value of an institution arising from adverse movements in interest rates that affect interest rate sensitive instruments, including gap [repricing] risk, basis risk and option risk.

ALCO assists management and the Board in managing the various elements of IRRBB. Interest rate risk is managed through matching assets and liabilities on the balance sheet with similar interest rate characteristics and by effecting interest rate swaps with external counterparties. The interest rate risk on fixed rate savings and mortgages is reviewed daily in Treasury, with hedging action taken as appropriate, within parameters defined in the FRMP.

Monthly, the balance sheet is stress tested to calculate the potential impacts on the Society's Economic Value and Net Interest Income in a variety of prescribed scenarios; the results are reported to ALCO and the Board.

3.2.2 Liquidity Risk

Liquidity Risk is the risk that the Society does not have sufficient financial resources available to meet its obligations as they fall due. ALCO assists the Society's management and the Board in managing this risk. Responsibility for the daily management of liquidity risk, including the monitoring of both retail and wholesale funding, lies with the Treasurer, within the framework prescribed by the FRMP. Monthly, the balance sheet is stress tested to confirm that the Group can withstand the extreme cash outflows likely to be experienced during either a firm-specific or marketwide liquidity shock. The liquidity stress testing regime is reviewed annually as part of the Internal Liquidity Adequacy Assessment Process (ILAAP) to ensure that all liquidity risk drivers (including those specified by the PRA) are considered. The ILAAP is an assessment of the Society's exposure to liquidity risk through to its planning horizon.

3.2.3 Funding Risk

Funding Risk is the risk that the Society does not have stable sources of funding in the medium and long term to enable it to meet its financial obligations, such as payments or collateral calls, as they fall due, either at all or only at excessive cost. The Society's savings and current account balances are higher than its mortgage balances reflecting deposit inflow during the current and previous year in excess of lending and excluding Term Funding Scheme with additional incentives for SMEs (TFSME) funding, it has a relatively low level of wholesale funding compared to many of its peers. Its deposits to loans ratio (the ratio of deposits from retail and SME customers to mortgage lending) was 107.6% at 31 March 2022. Of its £238 million in wholesale funding, £220 million was sourced through the Bank of England and £18 million comprised unsecured deposits derived from financial markets. Consequently, the Society's dependence upon the financial markets for funding is currently relatively limited.

3.2.4 Capital Risk

Capital Risk is the risk that the Society does not have sufficient capital to support its business activities. The Society maintains its capital at a level in excess of its regulatory Total Capital Required and internal limits. ALCO assists the Society's management and the Board in managing this risk. The Internal Capital Adequacy Assessment Process (ICAAP) is updated on an annual basis, it provides a qualitative and quantitative analysis of the Society's approach to capital risk management and includes a comprehensive internal assessment of the level of capital needed to support both risks faced under 'business as usual' and stressed scenarios.

3.3 Operational Risk

Operational risk is the risk of loss arising from inadequate or failed internal processes or systems, human error, external events or the underperformance or failure of third-party suppliers. The Operational Risk Policy sets out the Group's approach to the management of operational risk, with the Third-Party Relationship Policy covering the approach to the management of third-party risk.

Whilst line management is responsible for identifying and managing operational risks, this is carried out using an agreed framework and methodology and with the assistance of the Risk function, with quarterly reporting to the Operational Risk Committee (ORC), Risk Management Committee (RMC) and the BRC.

Various other Board-approved policies, e.g., the Group Information Security Policy, Financial Crime Policy and Data Protection Policy Statement, reinforce the Group Operational Risk Policy in specific areas.

The Society maintains appropriate insurance cover which is reviewed on at least an annual basis.

The Group's operational risk capital charge is calculated using the 'basic indicator approach'.

3.4 Conduct and Regulatory Risk

Conduct Risk is the risk that, unfair customer outcomes (i.e., harm) arise or may arise, from the operations of the Group and/or its third-party contractors. Regulatory Risk is the risk that the Society makes errors or exercises inappropriate judgement in the execution of its business activities, leading to non-compliance with regulation or legislation or voluntary codes of practice potentially leading to unfair outcomes for customers and/or regulatory sanction and/or reputational risks materialising. Conduct and regulatory risk is considered quarterly by the Conduct and Regulatory Risk Committee (CRRC). CRRC is a Management Committee which oversights specifically Conduct and Regulatory risk management across the Society. The CRRC reports to the RMC. On a quarterly basis, RMC reviews the Society's performance in this area, covering specific issues that have arisen and relevant management information as well as horizon scanning to ensure the requirements of changing regulation are captured. The RMC reports to the BRC, which in turn reports to the Board.

3.5 Strategic Risk

The Society's Board of Directors is responsible for the management of its strategic risk.

Strategic risk is the risk that the Society fails to adopt an appropriate business model, set appropriate goals and targets in the Corporate plan, adapt to external events or that the strategy fails to live up to expectations.

For a mutual building society, this covers the risks of failing to meet the requirements of its members in relation to their needs for financial services, of failing to retain them, and of failing to attract new members. It also necessitates balancing the interests of the two principal sets of existing members, borrowers, and savers, in relation to each other, and in relation to new members, so far as is possible given the trends in the wider market. Each quarter, the RMC, BRC and the Board consider formally, as an agenda item, the Society's key strategic risks which includes horizon scanning for regulation and other sources of change, and review of the wider political and economic environment.

To further enhance our understanding of Strategic Risk, during the year the society implemented a Climate Risk Management policy and framework, alongside a review of climate risk exposure and assessment of appropriate metrics to monitor risk. The risk is overseen by Board Risk Committee.

3.6 Pension Obligation Risk

The Society operates a defined benefit scheme (the Cumberland Building Society Pension and Assurance Scheme), together with three defined contribution schemes.

Pension liability risk attaches to the defined benefit scheme, in respect of a series of risks, including the potentially volatile course of the financial markets, the level of inflation and the effects of increasing life expectancy of scheme members. The scheme was closed to new members in 2000 and to future accrual at 31 March 2015.

Following a stress test of the assumptions relating to the scheme, the Society holds an additional amount of capital under Pillar 2 in recognition of this risk.

Further information on pensions is available in the Annual Report on page 37 and note 24.

4 Remuneration

4.1 Information relating to body that oversees remuneration

4.1.1 Composition and mandate of oversight body

The Society's objective in setting remuneration policies is to ensure that they are in line with its business strategy, risk appetite and long-term objectives, and that remuneration is set at a level to retain and attract individuals of the calibre necessary to operate an organisation such as the Society.

The Board has established a committee known as the People, Remuneration and Culture Committee (PARC) to assist in fulfilling its oversight and governance responsibilities in connection with its people, remuneration and cultural activities. The terms of reference of the Committee are available on the Society's website, *www.cumberland.co.uk* and include the following:

- Remuneration, culture, and people policies designed to support strategy and promote long term sustainable practice.
- Executive remuneration aligned to the Societies Purpose and Values and clearly linked to the successful delivery of the company's long-term strategy.
- A formal and transparent procedure for developing policy on executive remuneration and determining director and senior management remuneration. No director should be involved in deciding their own remuneration outcome.
- Directors should exercise independent judgement and discretion when authorising remuneration outcomes, taking account of company and individual performance, and wider circumstances.

Members of the PARC are appointed by the Board following consideration and recommendation by the Nomination and Governance Committee.

PARC membership comprises at least two further Non-Executive Directors in addition to the Chair. The Committee met 5 times during the financial year ended 31 March 2022.

4.1.2 External consultancy

The principles that underpin the Society's remuneration policy were initially developed as part of a third-party review by Praesto Partners LLP undertaken during the financial year. These were then reviewed by the Senior Leadership Team and then considered by PARC and adopted by the Committee. The development of principles to form the foundation of a more developed remuneration policy did not result in material changes but rather the review served to sense check and align to the People and Culture Strategy and the strategic aims of the Society.

The scope of our remuneration policy covers both the Society and Borderway Finance Limited, which is a wholly owned subsidiary.

4.1.3 Material risk takers (MRTs)

PARC has determined that there are 45 individuals (42 roles) who are material risk takers and whose professional activities have a material impact on the Society's risk profile.

The categories of employees cover:

- All members of the Society's Board (the Management body broken into its supervisory function – Non-Executive Directors and the Chairman, and its management function – the Executive Directors), senior leadership team and those receiving remuneration that takes them into the same remuneration bracket as senior managers and perform a professional activity within a material business unit of a kind that has a significant impact on the relevant business unit's risk profile. This includes Senior Management Function roles such as Chief Information Officer and Chief Operations Officer.

- Employees with managerial responsibility for business units, control functions, core business lines including those who could have a material impact on the company's risk profile such as General Counsel, Head of People and Culture, Head of Technology, and Head of Finance.
- Those whose professional activities have a material impact on the company's risk profile such as Head of Commercial and Head of Product.
- Those with authority to take, approve, or veto decisions on credit risk above a certain threshold such as Head of Underwriting.

4.2 Information relating to the design and structure of the remuneration system for identified staff

4.2.1 Overview of the key features and objectives of remuneration policy

Our approach to remuneration is designed to take into account the size, structure, nature of activity and the complexity of the activities performed by the Society. For our identified colleagues there is an alignment of remuneration to the risk profile of the Society to guard against inappropriate remuneration structures contributing to excessive and imprudent risk taking. Our remuneration design and structure are underpinned by a genuine understanding of the need to promote sound and effective risk management and considering the long-term interest of the Society.

We are not a large institution and therefore it is important we ensure our remuneration approach is simple to apply and administer. Fixed remuneration forms a high proportion of the reward package balancing a stable source of income with a modest element of variable pay of up to 20% of basic annual salary. This is blended with a benefits package which is designed to ensure our reward equation is balanced for all colleagues including those who are in our identified pool.

To develop and implement a strategic and effective approach to reward and recognition we believe that it is important for the Cumberland to be clear about the principles that underpin its reward strategy. Our People, Remuneration and Culture Committee approved a set of principles in January 2022 which act as a framework to assess existing reward arrangements, to assess the appropriateness of any proposed changes and provide a clear basis for employee communication about the reward and recognition strategy.

There are six reward principles:

1. Open and transparent;
2. consistent with our values;
3. recognises performance;
4. fair and consistent;
5. motivates and engages; and
6. proportionate and affordable.

These principles are to be used by the PARC to prompt and challenge reward decisions within its remit.

The reward principles are aligned to our People and Culture Strategy Recognise and Reward Pillar which outlines that:

- We will provide appropriate rewards for all our people.
- We will recognise people who live our values and produce good work.
- We will support our people to support our communities.

The decision-making process used for determining the remuneration policy and the role of the relevant stakeholders begins with the PARC who are responsible for setting the Society's Remuneration Policy for identified staff. This is supported by our Senior Leadership Team and informed by our internal control and corporate functions to ensure we have an appropriate and full informed professional approach. That holistic approach ensures we can apply policies and practices that are consistent across functions and that are clearly understood and applied.

4.2.2 Information on the criteria used for performance measurement and ex ante and ex post risk adjustment

The Society has in place a formal process of measuring performance using a framework called “Brighter Performance.” This process applies to every colleague role within the Society and is underpinned by a set of criteria drawn from the strategy of the Society and the clearly defined values. The overall setting and delivery of enterprise objectives linked closely to the strategy is determined annually by the Board. These form the high-level CEO objectives which are then cascaded through the business. This is led by each member of the Senior Leadership Team to ensure that their objectives are broken down into team and then individual objectives which are used to measure performance. These are reviewed at both individual level and Senior Leadership Team level and then, for senior management, at PARC through the balanced scorecard approach and are underpinned by the Brighter Performance process. This allows for a quarterly lighter touch review and then an end of year formal review, culminating in calibration of performance grades awarded. The CRO has a moderating role which allows for any risk adjustment to be made and discussed.

The shape of the calibration and any risk moderation receives oversight from the PARC which then reports at high level into the Board on an annual basis.

4.2.3 Information on how the institution ensures that staff in internal control functions are remunerated independently of the businesses they oversee

The internal control functions are independent and have sufficient resource, knowledge, and experience to perform their tasks and cooperate actively and regularly with each other. The remuneration of colleagues within the independent control functions allows for the employment of qualified and experienced colleagues and the reward equation is predominately fixed to reflect the nature of responsibilities in these areas.

Colleagues in control functions are part of the same Brighter Performance process as all other colleagues however care is taken to ensure that the methods used for determining any variable pay does not compromise their objectivity and independence. As such there is scope within the reporting structure for Board committee chairs to input into and moderate performance assessments to ensure any link to a remuneration award follows the remuneration principals and has not been unjustly measured in direct relation to the business they oversee. The PARC have oversight of the calibration process and are aware which roles within this universe fall within these criteria as part of their role within the annual approval of the Society’s methodology for identifying Material Risk Takers

*4.2.*4 Policies and criteria applied for the award of guaranteed variable remuneration and severance payments

There is no guaranteed variable remuneration and therefore there are no policies and criteria with respect to this.

The severance policy was developed by the People and Culture Team with third-party legal support and first approved by the People and Remuneration Committee in 2019. This has since been utilised for either planning or implementation in relation to organisation development work. The effectiveness of this policy was formally reviewed in January 2022 as part of the annual review process through the PARC and there are no material updates to the scheme.

The existence of such a policy allows for a consistent and appropriate scheme that ensures severance payments are dealt with in a consistent and fair way. This is underpinned by the principals of the reward policy. The policy is governed by the legal criteria that define the formal process and statutory award. There is a formula to enhance this on a consistent basis so that the minimum service requirements are available to all colleagues with over one years’ service (enhanced from the statutory entrance of two years’ service). In addition, the policy ensures all statutory redundancy payments are multiplied by a factor of two. This approach alongside carefully planned consultation and a wrap-around wellbeing ethos ensures that our values are upheld.

4.3 Description of the ways in which current and future risks are taken into account in the remuneration processes

The Society Risk register details the key risks which have been developed through both the Risk Management Committee and the Board Risk Committee these are reviewed on at least quarterly basis by both Committees. The Brighter Performance framework includes 5 strategic Pillars, one of which is “Protect the Society and our members” and all colleagues have related objectives. The Chief Risk Officer provides a risk view on all variable pay schemes.

4.4 The ratios between fixed and variable remuneration set in accordance with Article 94(1) of CRD

The ratios for annual variable remuneration range from 0-20% which ensures that no colleagues earn more than one third of the total annual remuneration in variable remuneration.

4.5 Description of the ways in which the institution seeks to link performance during a performance measurement period with levels of remuneration

4.5.1 Overview of main performance criteria and metrics for the institution, business lines and individuals

The approach measures and rewards performance by means of an incentive framework that links to the vision, purpose, and values of the Cumberland. The schemes are scored through two dimensions - “the what” and “the how”.

- “The what” (strategic objectives) has a weighting of 60% of the overall incentive achievement and is measured through delivering business/departmental plans, achieving objectives, and developing others.
- “The how” picks up the key dimension of how we deliver which is integral to the Cumberland (core values). This has a 40% weighting of the overall incentive achievement and is measured through assessment of performance against our values.
- This 60/40 ratio allows us to strive for delivering our strategic objectives whilst ensuring we adhere to our core values.

In summary the Scheme contains behavioural assessment against the values (What and How 60/40) and is subject to Calibration and a Chief Risk Officer assessment. There are both “what” and “how” gradings that result in a zero reward.

There is a maximum percentage award underpinning all our incentive schemes in line with regulatory requirements.

All incentives are underpinned by performance calibration. The practice of performance calibration refers to the steps taken to make sure that managers apply a consistent set of standards in making performance ratings.

The process ensures:

- A consistent set of End of Year appraisal ratings for those included in the annual incentive schemes.
- Assurance that People Managers have applied similar standards to all those included in the annual incentive schemes.
- Assurance that fair and objective performance appraisal of past performance is made in relation to others in similar roles and/or job levels who are included in the annual incentive schemes.

The measures include:

- Calibration of all colleague performance grades across the business against the Brighter Performance Process.
- Senior Leadership Team calibration for all Material Risk Takers.
- The CEO undertakes performance reviews with each member of the Senior Leadership Team, discussing the performance of each individual member of the SLT with the Chairman for counsel. This is then taken to the People Remuneration and Culture Committee (PARC) for oversight.

- The Chairman will carry out a performance review with the CEO.
- The CRO carries out an assessment of the Risk Management performance of those included in a variable pay scheme and identifies if there is moderation downwards required.
- The PARC annually reviews the shape of the calibrated grades reporting into Board thereon. A separate commentary is provided by the CRO, and the Committee has the opportunity to discuss this with the CRO. The output is a clear set of calibrated grades linked to payment under the framework with adjustment if appropriate for issues on risk management performance.

4.5.2 Overview of how amounts of individual variable remuneration are linked to institution-wide and individual performance

Our approach measures and rewards performance by means of an incentive framework that links to the vision, purpose, and values of the Cumberland. The schemes are scored through two dimensions - “the what” and “the how”.

- “The what” (strategic objectives) has a weighting of 60% of the overall incentive achievement and is measured through delivering business/departmental plans, achieving objectives, and developing others.
- “The how” picks up the key dimension of how we deliver which is integral to the Cumberland (core values). This has a 40% weighting of the overall incentive achievement and is measured through assessment of performance against our values.
- This 60/40 ratio allows us to strive for delivering our strategic objectives whilst ensuring we adhere to our core values.

In summary the Scheme contains behavioural assessment against the values (What and How 60/40) and is subject to calibration and a Chief Risk Officer assessment.

4.5.3 Criteria used to determine the balance between different types of instruments awarded including shares, equivalent ownership interest, options, and other instruments

Our only instrument is cash reflecting our mutual status and the absence of any listed capital market instruments.

4.5.4 Information of the measures the institution will implement to adjust variable remuneration in the event that performance metrics are weak, including the institution’s criteria for determining “weak” performance metrics

During the calibration process challenge is given as to the assessment of the performance of the colleague through a workshop approach where all colleague gradings are discussed within the contexts of both “what” has been delivered against objectives and “how” it has been delivered against the values. This is the criteria used to determine “weak” performance. In addition, a risk overview seeks to determine any other performance or behavioural themes that are to be taken into account. This seeks to form a fully rounded view on performance. Variable remuneration is then adjusted to take into account performance ensuring only those who exceed performance expectations receive their full variable incentive potential and in the same way identifying those whose performance does not meet the threshold for any variable reward. This provides for a rigorous and carefully controlled approach to awarding variable remuneration.

4.6 Description of the ways in which the institution seeks to adjust remuneration to take account of long-term performance.

4.6.1 Overview of the institution’s policy on deferral, pay-out in instrument, retention periods and vesting of variable remuneration including where it is different among staff or categories of staff

We do not have a policy on deferral, pay-out in instrument, retention periods and vesting of variable remuneration due to the levels and amounts of variable remuneration we have in place, the challenges inherent in our mutual business model which does not provide access to instruments in the way envisaged by regulatory rule makers, and the framework we have in place to reward variable pay.

Template UK REM1 - Remuneration awarded for the financial year

Table 8: UK REM1 - Remuneration awarded for the financial year

			a	b	c	d
			MB Supervisory function	MB Management function	Other senior management	Other identified staff
1	Fixed remuneration	Number of identified staff	7	2	6	30
2		Total fixed remuneration	345,950	597,502	931,350	2,592,372
3		Of which: cash-based	345,950	501,993	811,582	2,301,727
UK-4a		Of which: shares or equivalent ownership interests	-	-	-	-
5		Of which: share-linked instruments or equivalent non-cash instruments	-	-	-	-
UK-5x		Of which: other instruments	-	-	-	-
7		Of which: other forms	-	95,509	119,768	290,645
9	Variable remuneration	Number of identified staff	-	2	5	20
10		Total variable remuneration	-	100,399	93,058	127,902
11		Of which: cash-based	-	100,399	93,058	127,902
12		Of which: deferred	-	-	-	-
UK-13a		Of which: shares or equivalent ownership interests	-	-	-	-
UK-14a		Of which: deferred	-	-	-	-
UK-13b		Of which: share-linked instruments or equivalent non-cash instruments	-	-	-	-
UK-14b		Of which: deferred	-	-	-	-
UK-14x		Of which: other instruments	-	-	-	-
UK-14y		Of which: deferred	-	-	-	-
15		Of which: other forms	-	-	-	-
16		Of which: deferred	-	-	-	-
17	Total remuneration (2 + 10)		345,950	697,901	1,024,408	2,720,274

Template UK REM2 - Special payments to staff whose professional activities have a material impact on institutions' risk profile (identified staff)

Table 9: UK REM2 - Special payments to MRT staff

		a	b	c	d
		MB Supervisory function	**MB Management function**	**Other senior management**	**Other identified staff**
	Guaranteed variable remuneration awards				
1	Guaranteed variable remuneration awards - Number of identified staff	-	-	-	-
2	Guaranteed variable remuneration awards -Total amount	-	-	-	-
3	Of which guaranteed variable remuneration awards paid during the financial year, that are not taken into account in the bonus cap	-	-	-	-
	Severance payments awarded in previous periods, that have been paid out during the financial year				
4	Severance payments awarded in previous periods, that have been paid out during the financial year - Number of identified staff	-	-	-	3
5	Severance payments awarded in previous periods, that have been paid out during the financial year - Total amount	-	-	-	150,778
	Severance payments awarded during the financial year				
6	Severance payments awarded during the financial year - Number of identified staff	-	-	-	-
7	Severance payments awarded during the financial year - Total amount	-	-	-	-
8	Of which paid during the financial year	-	-	-	-
9	Of which deferred	-	-	-	-
10	Of which severance payments paid during the financial year, that are not taken into account in the bonus cap	-	-	-	-
11	Of which highest payment that has been awarded to a single person	-	-	-	-

Template UK REM5 - Information on remuneration of staff whose professional activities have a material impact on institutions' risk profile (identified staff)

Table 10: UK REM5 - Remuneration information on MRT staff

		Management body remuneration			Business areas						
		MB Supervisory function	MB Management function	Total MB	Investment banking	Retail banking	Asset management	Corporate functions	Independent internal control functions	All other	Total
1	Total number of identified staff										45
2	Of which: members of the MB	7	2	9							
3	Of which: other senior management				-	-	-	5	1	-	
4	Of which: other identified staff				-	8	-	17	5	-	
5	Total remuneration of identified staff	345,950	697,901	1,043,851	-	878,874	-	2,179,749	686,059	-	
6	Of which: variable remuneration	-	100,399	100,399	-	66,890	-	118,305	35,765	-	
7	Of which: fixed remuneration	345,950	597,502	943,452	-	811,984	-	2,061,444	650,294	-	

Attestation

Each of the Directors listed below, confirms that to the best of their knowledge that, the disclosures provided according to Disclosure (CRR) Part of the PRA Rulebook (CRR) Instrument 2021 have been prepared in accordance with the internal control processes agreed upon at the management body level.

Approved by the Cumberland Building Society Group Board and signed by their order.

Richard Ellison Chief Financial Officer 1 June 2022	Mark Stanger Audit Committee Chair 1 June 2022

Contact

For further information please contact:

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Appendix 1 – Capital resources statement

Table 11: UK CC1 - Composition of regulatory own funds

	Common Equity Tier 1 (CET1) capital: instruments and reserves	£'000
2	Retained earnings	202,096
3	Accumulated other comprehensive income (and other reserves)	3,008
UK-3a	Funds for general banking risk	-
UK-5a	Independently reviewed interim profits net of any foreseeable charge or dividend	-
6	**Common Equity Tier 1 (CET1) capital before regulatory adjustments**	**205,104**
	Common Equity Tier 1 (CET1) capital: regulatory adjustments	
7	Additional value adjustments (negative amount)	(61)
8	Intangible assets (net of related tax liability) (negative amount)	(2,462)
11	Fair value reserves related to gains or losses on cash flow hedges of financial instruments that are not valued at fair value	-
12	Negative amounts resulting from the calculation of expected loss amounts	-
14	Gains or losses on liabilities valued at fair value resulting from changes in own credit standing	-
15	Defined-benefit pension fund assets (negative amount)	-
25	of which: deferred tax assets arising from temporary differences	-
UK-25a	Losses for the current financial year (negative amount)	-
27a	Other regulatory adjustments to CET1 capital *(including IFRS 9 transitional adjustments when relevant)*	-
28	**Total regulatory adjustments to Common Equity Tier 1 (CET1)**	(2,523)
29	**Common Equity Tier 1 (CET1) capital**	**202,581**
57	**Total regulatory adjustments to Tier 2 (T2) capital**	**-**
58	**Tier 2 (T2) capital**	**-**
59	**Total capital (TC = T1 + T2)**	**202,581**

Appendix 2 – Reconciliation of accounting balance sheet assets to regulatory credit risk exposure

Table 12: Year-end balance sheet assets reconciled to regulatory exposures

	Group Balance Sheet Assets	Assets Deducted from Own Funds[7]	Provisions[8]	Regulatory off-balance sheet items[9]	Group Credit Risk Exposure[10]
Assets	**£'000**	**£'000**	**£'000**	**£'000**	**£'000**
Cash in hand and balances with the Bank of England	495,661	-	-	-	495,661
Loans and advances to credit institutions	45,686	-	-	-	45,686
Debt securities	55,025	-	-	-	55,025
Derivative financial instruments	34,037	-	-	-	34,037
Loans and advances to customers					-
Loans fully secured on residential property	2,040,274[11]	-	(605)	23,220	2,062,889
Other loans	191,020[11]	-	(2,141)	2,494	191,373
Investment in equity shares	6,717	-	-	-	6,717
Intangible assets	2,462	(2,462)	-	-	-
Tangible fixed assets	10,771	-	-	-	10,771
Investment properties	1,802	-	-	-	1,802
Other assets	2,117	-	-	-	2,117
Prepayments and accrued income	2,459	-	-	-	2,459
Total Assets	**2,888,031**[11]	**(2,462)**	**(2,746)**	**25,714**	**2,908,537**

[7] Under PRA rules intangible assets (including goodwill) must be deducted from regulatory capital.

[8] Provision as a credit risk mitigant

[9] Regulatory exposure of off-balance sheet items post credit conversion factor (CCF) relates to undrawn credit commitments for mortgages and other loans not yet drawn down.

[10] This does not include counterparty credit risk (CCR) exposure

[11] Gross exposure prior to provisions

Appendix 3 – Glossary of abbreviations and definitions

A	
ALCO (Assets & Liabilities Committee)	A committee which oversees treasury policy, financial risk management, capital, wholesale funding and liquidity.
B	
Basel II	Basel II is a set of international banking regulations put forth by the Basel Committee on Banking Supervision (BCBS), which levelled the international regulation of capital with uniform rules and guidelines. Basel II expanded rules for minimum capital requirements established under Basel 1 and provided the framework for regulatory review, as well as setting disclosure requirements for the assessment of capital adequacy of banks.
Basel III	An international regulatory accord that introduced a set of reforms designed to improve the regulation, supervision, and risk management within the banking sector.
BRC	Board Risk Committee
C	
CCF (Credit Conversion Factor)	The CCF converts an off-balance sheet exposure to its credit exposure equivalent which is then risk weighted. Off-balance sheet exposures have a probability of becoming a credit exposure and shifting onto the balance sheet. The CCF is an estimate of this probability, the expected value of the credit exposure is derived by multiplying the CCF with the value of the off-balance sheet exposure.
CCP (Central Counterparties)	Central counterparties (CCPs) are used in order to clear specified derivative transactions (predominantly interest rate swaps) thereby mitigating counterparty risk within the financial system. Positions are continuously marked and margin in the form of collateral is exchanged on at least a daily basis.
CCR (Counterparty Credit Risk)	The risk that a counterparty to a transaction will default before the final settlement of the transaction's cashflows.
CEO	Chief Executive Officer
CET1 (Common Equity Tier 1)	The highest form of regulatory capital under CRR, comprising common shares issued, related share premium, retained earnings and other reserves less regulatory adjustments.
CFO	Chief Financial Officer
CRD (Capital Requirements Directive)	The Capital Requirements Directive is an EU legislative package that contains prudential rules for banks, building societies and investment firms as onshored to the UK post Brexit and amended by applicable Statutory Instruments.
CRM (Capital Risk Mitigation)	Techniques such as collateral agreements used to reduce the credit risk associated with an exposure.

CRO	Chief Risk Officer
CRR (Capital Requirements Regulation)	The Capital Requirements Regulation is an EU law, which was onshored to the UK post Brexit and amended by relevant Statutory Instruments. The CRR aims to decrease the likelihood that banks become insolvent, reflecting Basel III rules on capital measurement and capital standards.
CVA (Credit Valuation Adjustment)	Adjustments to the fair value of derivative assets to reflect the credit worthiness of the counterparty.
E	
ECAI (External Credit Assessment Institutions)	An ECAI (For example Moody's, Standard and Poor's, Fitch) is an institution that assigns credit ratings to issuers of certain types of debt obligations as well as the debt instruments themselves.
F	
FCA (Financial Conduct Authority)	The UK regulatory body responsible for conduct of business regulation and supervision of UK authorised firms. The FCA is also responsible for the prudential regulation of firms which do not fall within the scope of the PRA.
FRMP	Financial Risk Management Policy
G	
GHOS (Group of Central Bank Governors and Heads of Supervision)	The GHOS is the oversight body of the Basel Committee, the primary global standard setter for the prudential regulation of banks.
H	
HQLA (High Quality Liquid Assets)	The high-quality liquid assets (HQLA) include only those with a high potential to be converted easily and quickly into cash (in times of distress). HQLA are cash or assets that can be converted into cash quickly through sales (or by being pledged as collateral) with no significant loss of value.
I	
ICAAP (Internal Capital Adequacy Assessment Process)	The institution's own assessment of the level of capital needed in respect of its regulatory capital requirements (for Credit, Market and Operational Risks) and for other risks including stress events.
ILAAP (Internal Liquidity Adequacy Assessment Process)	The institution's own assessment of the level of liquidity needed in respect of its regulatory requirement to ensure that the Group maintains adequate liquid assets to survive a defined stress scenario for a sufficient period as defined by Risk Appetite.
IRRBB (Interest Rate Risk in the Banking Book)	IRRBB is the current or prospective risk to both earnings and economic value arising from movements in interest rates. The main sub-types of IRRBB include gap risk (or repricing risk), basis risk and customer optionality risk.
L	
LTV (Loan To Value)	A ratio which expresses the amount of a mortgage as a percentage of the value of the property on which the mortgage is secured. The Group calculates residential mortgage LTV on an indexed basis (the value of the property is updated on a quarterly basis to reflect changes in the house price index (HPI))

M	
Minimum Capital Requirement (MCR)	The minimum amount of regulatory capital that a financial institution must hold to meet the Basel III Pillar 1 requirements for credit, market, and operational risk.
N	
NSFR (Net Stable Funding Ratio)	The NSFR is defined as the amount of available stable funding relative to the amount of. required stable funding.
P	
PARC	People Remuneration & Culture Committee
PRA (Prudential Regulation Authority)	Responsible for the prudential regulation and supervision of banks, building societies, credit unions, insurers, and major investment firms in the UK. The PRA is a subsidiary of the Bank of England.
Pillar 1	The first pillar of the Basel II framework sets out the minimum regulatory capital requirements (8%) for Credit, Market and Operational Risks.
Pillar 2	The second pillar off the Basel II framework, known as the Supervisory Review Process, sets out the review process for a bank's capital adequacy; the process under which supervisors evaluate how well banks are assessing their risks and the actions taken as a result of these assessments.
Pillar 2A	Pillar 2A addresses risks to an individual firm which are either not captured, or not fully captured under the Pillar 1 capital requirements applicable to all banks.
Pillar 3	The third pillar of the Basel II framework aims to encourage market discipline by setting out disclosure requirements for banks on their capital, risk exposures and risk assessment processes. These disclosures are aimed at improving the information made available to the market.
R	
Risk Appetite	The level and types of risk that a firm is willing to assume to achieve its strategic objectives.
RMC	Risk Management Committee
RMF	Risk Management Framework
RWA (Risk Weighted Assets)	Calculated by assigning a degree of risk expressed as a percentage (risk weight) to an exposure value in accordance with the applicable Standardised Approach.
S	
SLT	Senior Leadership Team
SME	Small to Medium Enterprises

SREP (Supervisory Review and Evaluation Process)	The PRA assessment of a firm's own individual capital assessment under Pillar 2.
Standardised Approach	In relation to Credit Risk, the method for calculating Credit Risk capital requirements using risk weightings that are prescribed by regulation. Standardised Approaches, following prescribed methodologies also exist for calculating Market and Operational Risk capital requirements.
T	
TFSME (Term Funding Scheme with additional incentive for SMEs)	Funding schemes provided by the Bank of England which provide participating banks and building societies with funding at interest rates close to Bank Rate. The Group has specifically utilised both the original Term Funding Scheme (TFS) and the more recent Term Funding Scheme with additional incentives for SMEs.
Tier 1 Capital	A component of regulatory capital, comprising Common Equity Tier 1 capital and Additional Tier 1 capital. Additional Tier 1 capital includes qualifying capital instruments such as non-cumulative perpetual preference shares and Additional Tier 1 capital securities.
Tier 2 Capital	A component of regulatory capital, comprising qualifying subordinated loan capital and related non-controlling interests.