Annual report and financial statements

30 September 2021

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F.C.A.

Jan Preece
Director
Chief Financial Officer
A.C,A.

Helen Molyneux
Non-Executive Director
L.L.D (Hons), L.L.B (Hons)

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Non-Executive Director
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Aileen Wallace
Non-Executive Director
M.C.B.I, C.I.R.M. A.M.B.C.S.

Iain Laing
Non-Executive Director

Kirsty Williams
Company Secretary
L.L.B. (Hons).

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Strategic report

Chairman's Statement

> The focus of the year has been one of continued strategic alignment of the Bank behind our Retail ambitions.

The focus of the year has been one of continued strategic alignment of the Bank behind our growth ambitions whilst the management team has provided excellent leadership and direction to colleagues to deliver improved service during the extended challenge presented by the COVID-19 impact on customers and markets alike. The response from colleagues across all of our teams was exemplary and the Board would like to place on record our sincere appreciation to all colleagues who stepped up to the challenge with such tremendous professionalism.

At a Group level, the Board agreed with the Shareholder the sale of the Hodge Life Assurance Company ('HLAC') following extensive assessment of our longer-term options and this provides an opportunity for the Bank to access capital in the coming months to facilitate its ambitious growth plans which will ultimately create significant value and a greatly enhanced customer experience.

During the year, the Board undertook a deep dive into the 5-year strategic plan led by the executive management with the support and challenge of Fenchurch Advisory Partners. The focus of the plan is to grow the retail balance sheet primarily in specialist mortgages, building on the experience and expertise that exists in the Bank, alongside creating a truly digitally enabled savings franchise which will see Hodge offering a broader range of savings propositions to a wider customer market. The Bank is also exploring options to utilise the experience and skillset that exist within the Commercial team to utilise surplus additional capital in a value enhancing way.

Whilst the goals are ambitious, benchmarking confirms that the ambitious balance sheet growth, return on capital and profitability are achievable and realistic, and so the Board and Shareholder were happy to endorse the plan and to provide the investment and resources needed to deliver the strategy.

The Board also agreed the strategic direction of the Bank in respect of our environmental, social and governance ('ESG') goals for the 5-year plan following an extensive review led by the executive team, with the expertise and insight of KPMG.

Our initial commitment made to support ESG was for Hodge to achieve carbon neutrality for direct emissions from operations by the end of 2021. Following support from the Carbon Trust, in understanding our footprint, a further commitment has been made to progress work in understanding downstream emissions such as scope 3 financed emissions. In doing so, this will then allow a credible transition plan to be developed, ensuring that the social initiatives of Hodge continue to develop and mature. We will show more public disclosure of these through the Hodge website and ensure they are supported through our purpose.

Returning to focus on the current year, there has been encouraging

Chairman's Statement (continued)

progress made in improving the customer experience and in growing the mortgage balances despite the continued challenge presented by COVID-19.

A key deliverable under the 5-year strategy is to provide a high level of customer experience, one that benchmarks in top quartile against our key competitors. In order to enable this, we have created a dedicated Customer Experience team who have introduced the tools and technology to assess how and when experiences fall short of our standards and to work across the business to make immediate and sustainable changes. This has seen some very immediate results, nowhere better illustrated than in our savings proposition where we have seen nearly 80% of customers rating the Bank as 5* via Trustpilot.

The growth in mortgages has been very promising, with a series of record new business levels month on month, reflected in the growth in the residential mortgages balance sheet of over £332m, a 95.7% increase year on year.

The management team have delivered on our plans to start servicing mortgages in house, with a new Business Operations team and mortgage servicing platform. This is a critical step in improving the customer experience, increasing agility and flexibility and managing our operational costs.

Alongside this, new capabilities have been developed to enable repayment facilities as well as the launch of the holiday lets product range, both key to our growth strategy.

Whilst there is still a considerable amount of investment necessary in the savings business, we have seen a 28.9% increase in savings balances during the year. The direction is clear; to develop the digital proposition, and the investment in this has begun with a raft of improvements to the savings journey, all driven by feedback from our customers.

The expertise and capabilities in the technology teams has meant that in many cases these changes went from 'ideation' to live in a matter of weeks, as the teams have developed their ability to deliver change quickly and without disruption.

Looking forward, we have started to build the foundations for our future savings proposition, through deciding to replace one of a very few remaining legacy parts of our application estate with Mambu, a modern software as a service ('SaaS') cloud native core banking platform. Mambu will allow us to move ahead at a far greater pace and deliver the customer experience and product offerings needed to support the business strategy.

'Behind the scenes' we have continued to invest heavily in making sure that our customers data continues to be protected from the ever-changing cyber security threat landscape, along with heavy focus on risks presented from our supply chain.

In light of the revised business strategy, we have revised our information systems strategy for the business plan for the period ahead, setting out how we will leverage technology to augment and free up the human element in customer interactions where intervention from our colleagues can add the most value.

The revised strategy was subjected to an external review, which confirmed that it set out a direction which aligns with 'best of breed' strategies within the market and clearly aligns with Hodge's strategic intent. The Board and Shareholder were happy to approve the strategy.

Our continued improvements in risk management have seen further investment into 1st line risk management in the retail area, strengthening of credit risk capability across both 1st line and 2nd line of defence, refinement of risk taxonomy and overhaul of supporting principal risk management frameworks, and embedding and maturing our understanding and assessment of risks associated with climate change.

Finally, and following on from the significant appointments of David Landen as CEO and Matt Burton as Retail Director at the latter part of last year, we are delighted to have appointed Janet Preece as CFO.

The NEDs have provided a high level of support and challenge during the year and I am confident that we have a highly professional and effective board which will ensure that the strategy is subject to robust and prudent oversight.

Alison Halsey sadly resigned from her post in August for personal reasons. The end of this year will also see the retirement of Helen Molyneux from the Board after many years of invaluable insight, challenge, mentoring and counselling support. Helen has been most instrumental in our Colleague agenda, both as Chair of Remuneration Committee but also as the Board Member assuming responsibility for Colleague wellbeing and engagement. Helen leaves with the thanks and appreciation of all Board Members but from me in particular as Chair.

Given the changes to the Group following the sale of Hodge Life, we will not be replacing Helen on the Board but will realign responsibilities, with Aileen Wallace assuming the role as Chair of Remuneration Committee from the new year.

Graeme Hughes
Chairman
6 December 2021

Our Business, Social Responsibility and Stakeholder Engagement

We are a privately owned bank seeking to make life better for customers and society in the moments that matter.

What we do

Hodge is a specialist UK lending and savings bank focused on specialist finance and savings. We differentiate ourselves by concentrating on markets where our expert knowledge, judgement and personalised approach to lending offer us a competitive advantage.

Residential mortgages

The Bank's specialist mortgage business is focused on complex income, later life lending and holiday buy-to-let.

We work closely in partnership with our trusted network of intermediaries, serving customers looking to invest in a holiday home through our holiday let mortgage, and personal customers through our complex income and later life mortgages.

Our range of residential mortgages allow customers to either repay down the capital or choose interest only. Our interest only mortgages allow customers to repay the mortgage with or without a fixed-term end. Our later life mortgages are available to those over 50, a growing market that we are committed to serving.

2021 has been a year of focus, continuing to build on the service delivery improvements we made in 2020 and continuing to place our customers at the heart of everything we do. We continue to grow with new lending up 95.7% on the prior year, in 2022 we will continue to launch into new specialist areas. We will continue to invest in the intermediary experience with the launch of our retention platform during this year. We continue to engage, value and respond to feedback from the broker community, delivering a range of product updates and service enhancements throughout the year. We work closely with them to ensure the products we offer deliver for our customers whilst providing flexibility in a notoriously rigid market.

This is essential as we continue to evolve our product offering in 2022.

We have also committed significant investment in our team, strengthening our expertise and capability to serve and respond to the market. This continues to pay dividends in the feedback we receive from brokers.

Commercial lending

Our core purpose is to support experienced, serially active investors and developers of real estate assets, in residential schemes. This means that we impact positively on the communities into which we lend, by helping our clients deliver much needed new homes for sale or rent, as well as regenerating areas.

2021 has been a year of challenge impacted by the ongoing uncertainty around the COVID-19 pandemic. Nevertheless, we have delivered an operating profit in line with our forecasts of £3.9m despite closing to new business for Q1 and Q2 as market uncertainty prevailed.

During that downtime, we have made significant changes to our business model to sustain our growth both during and after the pandemic. This has involved revising our credit policy in line with our updated strategic direction, reconfiguring our products, and refreshing the team structure to align to our proposition and client needs. To secure sustained growth, we have created a proposition function and product pipeline to deliver our future plan volumes.

In the second half of the year as the wider economy reopened and confidence levels rebounded, we opened up to new business. We're pleased that our updated offering has proved attractive to our target market to date. We are growing our lending volumes and securing new clients, whilst continuing to service our existing client base.

Our clients remain central to everything we do and we are continuing to invest time, effort and money in improving the efficiency of our systems, processes and people as we strive for excellent client experience across all areas of our business.

Savings

Customer savings are, and will remain to be, the most important part of our funding base.

Throughout 2021 we have continued our commitment to support more customers through our online channels. Continued investment in digital capabilities, simplifying processes and leveraging technology to quicken our service is driving positive feedback from current and new customers evidenced in our 'excellent' Trust Pilot score.

During the next twelve months we aim to make significant investment in our technology infrastructure to provide a leading digital experience to give our customers even more control over how they engage with us. Whilst allowing customers more flexibility to manage their finances, we will provide an experience that is simple and easy but also personalised in the moments that matter. We know that our customers appreciate the value of human touch and that is why we will continue to ensure our experts are available to answer any queries.

We continue to manage over £1bn of our customers' savings balances and will continue to grow our presence in the personal savings market providing an excellent digital experience, attractive interest rates and products and services that meet our customers' needs.

The Bank is also a participant in the Bank of England's Term Funding Scheme ('TFSME'), which provides a cost-effective source of funding

Our Business, Social Responsibility and Stakeholder Engagement (continued)

in the form of central bank reserves to support additional lending to the real economy. The TFSME balance represents 10% of the overall funding from deposits with banks and customers at 30 September 2021.

Colleagues

Our people are central to the value we deliver for our customers and the key to creating a strong experience for our customers. We remain committed to building a culture where people thrive through rewarding talent and performance.

- **Learning and Development:** Throughout this year we have continued to develop our learning platform and range of development programmes with over 150 available to support our colleagues and help them flourish and grow in their careers at Hodge. We have invested in our leadership development offering a range of Institute of Leadership Management ('ILM') leadership and coaching qualifications. Whilst also investing in the technical skills across the business to support our Customer Experience ('CX') programme, financial and fintech capability. We continue to support our future talent through our internal succession talent plans and the Welsh Financial Services Graduate programme, for 'rising stars' in the business and supporting career paths and progression which has created new opportunities for many of our team.
- **Colleague Wellbeing:** We have continued to support our colleagues through our 'Healthy Hodge' scheme, providing resources and support for maintaining healthy minds, bodies, families, finances, and connections. Investing in a range of training programmes to increase our mental health awareness and support our hybrid working approach for our leaders and colleagues. Even prior to the availability of working space at One Central Square, we ensured we kept an option open for those colleagues who needed to work at the office for any wellbeing reasons.
- **Flexible Benefits:** The foundation set by the introduction of flexible benefits has been built upon over the last year. We have strengthened the processes and frameworks we have in place around reward & recognition, drawing a stronger link between reward and performance / competency for colleagues. Moving into the new year we will review our flexible benefits offering again with colleagues, allowing us to ensure we have the most effective package we can for current and future colleagues.
- **Inclusivity & Flexibility:** Building on successes from the previous year, we have been working towards further improvements that will see us make further strides towards being a truly inclusive workplace. Through our core hybrid working model, flexibility remains a key aspect of that as a commitment to empowering our people to work in a way that works for them as often as possible. Alongside this, we are exploring ways to embed a culture of supportive allyship across all teams at Hodge. We formed a new Equality, Diversity & Inclusion ('ED&I') network with members from across the business to widen the focus of inclusivity across all facets which can impact the feeling of exclusion.

  We hope that this would help to increase representation across Hodge, and we have a good signal that this will work as more colleagues continue to update their Diversity and Inclusion ('D&I') data fields in the HR system. The percentage of colleagues who have provided no data is now below 25%, having been around the 40% mark at the start of this year. The number of colleagues who previously stated 'prefer not to say' in all their ED&I fields has also halved since the beginning of the year.

Corporate Social Responsibility

Throughout 2021 we have deepened our commitment to helping older people live safely. Working closely with Hourglass, the only UK charity committed to preventing abuse against older people, we are working together to raise awareness and provide better support where it's needed, including helping our teams understand more around the particular issue of financial abuse, how to spot it and how we help.

Our Business, Social Responsibility and Stakeholder Engagement (continued)

Stakeholder Engagement – S172 Statement

The Companies Act 2006 requires the directors of the Bank to act in the way he or she considers, in good faith, would be most likely to promote the success of the Bank for the benefit of its stakeholders as a whole. In doing so, s172 requires a director to have regard, amongst other matters, to the:

- likely consequences of any decisions in the long-term;
- interests of the Bank's employees;
- need to foster the Bank's business relationships with suppliers, customers and others;
- desirability of the Bank maintaining a reputation for high standards of business conduct;
- impact of the Bank's operations on the community and environment; and
- interests of the Bank's Shareholder.

In discharging its s172 duties, the directors of the Bank have regard to the factors set out above. The Board also has regard to other factors which it considers relevant to the decisions it makes. The Board acknowledges that not every decision it makes will necessarily result in a positive outcome for all of the Bank's stakeholders. By considering the Bank's purpose, vision and values together with its strategic priorities and having a process in place for decision-making, the Board does, however, aim to make sure that its decisions are consistent.

The Board delegates authority for the day-to-day running of the business to the Bank's CEO and, through him, to the Executive Committee to set, approve and oversee the execution of the Bank's strategy and related policies. The Board reviews matters relating to financial and operational performance, business strategy, key risks, stakeholder-related matters, compliance and legal and regulatory matters, over the course of the financial year. This is supported through the consideration of reports and presentations provided at board meetings and reviewing aspects of the Bank's strategy at least twice a year. A high-level summary of the Bank's strategy can be found in the Chairman's Statement on page 8.

The Bank has a number of key stakeholder groups with whom it actively engages. Listening to, understanding and engaging with these stakeholder groups is an important role for the Board in setting strategy and decision-making. The Bank recognises its obligations and requirements to be a well-controlled financial services business, compliant with regulation and delivering good customer outcomes. The Regulators are consulted and kept closely informed in relation to key decisions made by the Board, as appropriate. A summary of how the Board engages with customers, employees, suppliers, the community, and the Shareholder is provided below:

Our Customers

As a customer-centric business the Bank uses a range of methods to involve and engage with our customers. The Board values feedback from customers to ensure the Bank is providing them with what they want and need.

The Bank has an established customer experience function to drive customer obsession and continues to work closely with our broker community to ensure the products we design are needed and add value for customers. We capture feedback through a variety of surveys and capture reviews through Trust Pilot as an independent measure of our service and experience as and when customers interact with the Bank.

2021 has been a year of continued progress as we accelerate our commitment to putting the customer at the heart of everything we do. We have engaged our customer and broker communities in the evolution of our product and service offerings, continuing to champion the needs of our audiences in helping them achieve their goals and ambitions.

Hodge continues to invest heavily in technology to improve our operational and digital capability which is vital in delivering great service to our customers. This investment brings efficiency and scalability to our operations. In 2021, the Bank has invested in a new banking platform that will underpin our entire business model, improving efficiencies and capabilities for our teams, whilst delivering first class experiences to our customers. Together with a new online savings application journey that we've invested in, 2022 will see further enhancements to our offering.

Our Employees

We continue to invest in our people, with leadership support and mentoring across the business. This commitment will enhance strategic leadership as well as strengthening capability at multiple levels throughout the organisation.

Throughout 2021, continued uncertainty surrounding the COVID-19 pandemic has reinforced our efforts in building colleague engagement through a range of communication channels, as well as via several colleague representative groups. Keeping our teams safe and empowering them to continue to provide for our customers remains our priority through.

During the year, a consultation with employees of the Bank was held around the pension scheme. Following the consultation, it was decided to close the defined benefit scheme to further accrual and to replace it with a new defined contribution scheme for all employees.

Our Business, Social Responsibility and Stakeholder Engagement (continued)

The Board has appointed a designated non-executive director to assist with providing a link between employees and the Board. Helen regularly attends colleague engagement meetings as a Board representative and provides a summary to the other directors on the output of such meetings.

Our Suppliers

Our suppliers play an important role in the operation of the Bank's business to enable the delivery of an effective and efficient business model. We continue to see benefits from investing in a new procurement system in 2020, improving the due diligence, procurement process and the management of the relationship with our suppliers.

During 2021 several material contracts were presented to the Board for approval, covering both new relationships and contract renewals. In approving these contracts, the Board considered the strategic value of the relationships as well as looking at the customer impacts, risk exposure, legal and compliance considerations and financial implications. The Bank has a framework in place which provides a consistent and proportionate approach to the procurement and management of suppliers to ensure that it can effectively engage, manage and terminate, where appropriate, supplier relationships.

Our Shareholder

A Shareholder Engagement policy has been agreed and adopted by the Board, detailing the Shareholders' expectations of the Bank and those matters that require shareholder approval or shareholder consultation, to support appropriate Governance and oversight.

The Board provides updates to and engages with the Shareholder of the Bank regularly to obtain a clear understanding of its views and requirements.

Our Community

Throughout 2021 we have continued to make a difference to the lives of others through our corporate social responsibility commitment. The Bank has a focus on supporting older people live safe lives through partnering with Hourglass. Additionally, every member of our team benefits from up to four days off work per year to support good causes with the Bank's 'Four to do More' initiative.

Our Business, Social Responsibility and Stakeholder Engagement (continued)

The Environment

A Climate Change policy is being developed outlining governance structures, disclosures, risk management approach and the SMF responsibility in the business. An internal working group is also being established to develop the Bank's approach and understanding of the risk posed by climate change. Climate change is also being considered specifically as part of the regulatory risk management documents; Internal Capital Adequacy Assessment Process ('ICAAP') & Internal Liquidity Adequacy Assessment ('ILAAP').

The Bank is reporting Green House Gas ('GHG') emissions for the first time in FY21 to comply with the Streamlined Energy & Carbon Reporting (SECR) initiative.

We tasked The Carbon Trust to calculate our GHG emissions under the rules laid out by the World Resources Institute's GHG Protocol Corporate Accounting and Reporting Standard. This enables us to ensure the accuracy of these disclosures and to monitor our own performance in reducing our carbon footprint. We are focused on making the Bank a more sustainable organisation, both in terms of our carbon footprint and the products that we offer. The figures are for the year to June 2021.

Scope 1 – direct GHG emissions

Includes emissions from activities owned or controlled by the Bank that release emissions into the atmosphere. Examples include emissions from combustion in owned or controlled boilers, vehicles.

Scope 2 – energy indirect emissions

Includes emissions from own consumption of purchased electricity, heat, steam and cooling. These are a consequence of the Bank's activities but are from sources not owned/ controlled.

Scope 3 – other indirect emissions

Emissions that are as a consequence of the Bank's actions, but the source is not owned or controlled, and which are not classed as scope 2 emissions.

Scope	GHG Emissions Source	2021
Scope 1 (tCO2e)	Fuel (Buildings)	5.0
	Fuel (Owned vehicles)	-
Scope 2 (tCO2e)	Electricity	17.0
	Company electric vehicles	-
Scope 3 (tCO2e)	Business Travel	2.6
	Employee Commuting	144.8
	Other	0.1
Total location based GHG emissions (tCO2e)		169.5
Average number of employees		321.0
GHG per employee (tCO2e)		0.53
GHG use per £m income (tCO2e)		28.3

All of the Bank's operations are UK based. The Bank's GHG emissions are reported in (tCO2e) and usage in (kWh). GHG emissions per employee and income are reported as intensity metrics, for future ease of comparison.

Chief Executive Officer's Statement

> It's a huge privilege to present the Hodge financial statements for my first full year as CEO.

It's a huge privilege to present the Hodge financial statements for my first full year as CEO. It's been a year of great change at Hodge as we continue to invest in the organisation to deliver our exciting future growth plans. I look back on the year with immense pride in all that we have achieved in such challenging circumstances. Of course, none of our achievements this year would have been possible without our fantastic people. In a year with most of our colleagues remaining at home, I'm so proud of the level of service provided.

The wellbeing of colleagues has been our top priority; after the sudden impact of disruptions due to COVID-19 in FY20, we entered FY21 with a clearer picture of what would be required to support our colleagues who are still predominately working from home.

One of the most important factors was to ensure that all colleagues, no matter where they were working, always had easy access to resources or support channels. Our 'Healthy Hodge' wellbeing approach, which we originally introduced in 2018, has evolved to fit the needs of a physically disconnected workforce. We continued to invest in our leaders, providing them with mental health awareness training to ensure that they were given support to be able to support their teams. We also doubled the number of qualified mental health first aiders at Hodge, with 18 of these available across the business. We also used these key groups to participate in a range of colleague communication sessions where we continued to remind and encourage colleagues to make use of flexible working options and resources to look after their own wellbeing.

While most colleagues were working at home through FY21, we still ensured we had safe working spaces available at our One Central Square office and we are looking to the future as we adapt how we work to respond to the changes witnessed over the last 18 months. We will be adopting hybrid working allowing colleagues to work from where best it is to work; the office though retains a hugely important role in the culture of Hodge, and we are expanding our office footprint to allow for a working environment that cultivates collaboration and allows colleagues to learn and develop in their roles.

Customers

Our business wouldn't exist if it wasn't for our customers, and we strive to serve them better each day. As I will outline later, our technology investment is focussed on offering more functionality and offerings for our customers and our fantastic customer service teams continue to provide an amazing personal service when our customers need it most. We always strive to be better, and we continue with that mindset, but we are incredibility proud of what our customers are telling us, with a strong Trust Pilot score showing we are providing that great service we strive for every day.

The markets we operate in are, by their nature, specialised and whilst

Chief Executive Officer's Statement (continued)

technology still plays a huge part, we pride ourselves in allowing our customers and intermediary partners the ability to speak to us in the moments that matter, whether that be a significant moment in their lives, to discuss their experience with Hodge or to better understand the products we offer, hence the ability to communicate with us is key.

The Hodge Life Assurance Company Limited sale

During the year Hodge Limited, the Bank's parent, completed the sale of the Hodge Life Assurance Company Limited ("Hodge Life") to the Reinsurance Group of America. Hodge colleagues supported this sale process, and we are delighted to have reached a successful completion. The transaction enables the Bank to move forward confidently with our ambitions to become a real specialist bank delivering fantastic products to our customers and underpinning our ambitious growth plans over the coming years.

Business performance

I am delighted to introduce Janet Preece, who has joined us to become our new CFO, Jan brings a wealth of experience across financial services and will be a fantastic addition to the team, Jan will present in more detail the financial highlights.

As planned, 2021 has been a year of transition, with the significant balance sheet restructuring having taken place it sets us up for our future growth plans. During the year along with the successful Hodge Life sale we have also sold the final portfolio of equity release mortgages and following the year end we are planning to sell the home reversion portfolio; these two sales are the final elements of the balance sheet restructuring and will mean the volatility in our results seen in the past will be greatly reduced; as well as freeing up funds to support continued growth in our core markets.

Our mortgage business has performed extremely strongly helped by the strong housing market, our product offerings and the service delivered by our teams to intermediaries and customers. New completions in residential mortgages held at amortised cost during 2021 were £332million (2020: £168million) a year-on-year increase of 95.7%, some of this was due to market factors such as the stamp duty holiday and the pent-up demand because of the 2020 lockdown but it also represents the efforts of our teams to build the awareness in the markets we serve.

Our savings business continues to grow to support our wider ambitions; we have focussed our savings offering to enable us to really be a personal savings business of choice, delivering great products and services to our customers. Our savings balances have increased from £1,071.4m in 2020 to £1,381.0m in 2021 with a significant growth in customer numbers.

Our technology investment continues apace; providing new functionality for our customers and enabling us to serve our customers more efficiently.

Our mortgage platform which went live in April 2020 continues to be enhanced improving our intermediary partners experience, 98% of our business has been introduced via our platform since launch.

We have delivered significant improvement to our savings business and have also agreed to implement the Mambu savings platform which we are incredibility excited to announce given the functionality this will enable us to provide to our customers.

Safety

Our capital, the amount of money we have to protect us from potential losses, remains extremely robust with our Common Equity Tier Ratio of 20.2% providing a solid foundation to implement our growth strategy. This has benefitted from the restructuring of the balance sheet and the move toward lower risk specialist mortgages.

Liquidity levels have also remained strong with our LCR standing at 349.6% at the year-end showing we have significant levels of surplus liquidity to fund our growth. During the year we have drawn down on the Bank of England's Term Funding Scheme ('TFSME') to further diversify our funding sources and demonstrating our commitment to growth.

Environment

As we all know the world is facing its biggest challenge; the need to be carbon neutral by 2050 to prevent the continued global warming we have witnessed over the last 100 years. Hodge is committed to being an organisation that contributes back to society, we have partnered with a third party to understand our own carbon footprint; to understand better the risks facing Hodge and are now working on ways we can support our customers to improve the efficiency of homes, vital if the UK is to meet its targets.

The future

I am incredibility excited for the future; the work undertaken through COVID-19 to simplify our business, focus on what we do best and build an organisation that can grow, sets up for a hugely exciting period as we grow our business to meet our ambitious plans.

David Landen
Chief Executive Officer
6 December 2021

Chief Financial Officer's Report

Despite 2021 remaining a challenging year... ...the Bank increased its loans and advances to customers.

Despite 2021 remaining a challenging year, with the ongoing economic environment caused by COVID-19, the Bank increased its loans and advances to customers at amortised cost by 40.4% and its deposits from customers by 28.9%.

Key performance indicators
The Bank monitors several key performance indicators to measure progress against objectives and to demonstrate financial soundness.

During 2020, the Bank changed its reporting period from 31 October to 30 September as Hodge staff have previously been operating under pressure to complete the financial statements in the lead up to the December holiday season. Hence the 2021 period on the right is comparing a 12-month period with an 11-month period:-

Chief Financial Officer's Statement (continued)

	2021	2020
Financial performance	**£m**	**£m**
Net interest income	17.6	15.6
Net operating income	26.2	20.9
Operating loss	(2.1)	(8.6)
Profit / (loss) before tax	3.7	(21.1)
Group financial ratios	**%**	**%**
Net interest margin[1]	1.0	1.1
Cost to income ratio[2]	98.9	106.7
Financial soundness	**%**	**%**
Common Equity Tier 1 ratio[3]	20.2	19.7
Leverage ratio[4]	8.3	9.6
Liquidity Coverage ratio[5]	349.6	272.9

1 Net interest margin: net interest income as a proportion of total assets.
2 Cost income ratio: administration expenses; as a proportion of net operating income.
3 Common equity Tier 1 capital divided by total risk weighted assets.
4 Common equity Tier 1 capital fully phased in definition divided by total exposure.
5 High quality liquid assets divided by net cash outflows over 30 days calculated in line with the delegated act.

The Bank's performance at a net interest income level improved during the year as the Bank continued with its planned growth in residential mortgages. The residential mortgages increase has been offset slightly by the reduction in commercial lending balances and the sale of the equity release mortgage portfolio.

The Bank's performance at an operating loss level improved by £6.5 million as a result of the planned growth in residential mortgages, noted above, but also due to proportional decreases in provisions as the economy recovers from the initial shock of COVID-19. There's also been an improvement in investment income during the year as a result of the residential property market reopening leading to increased sales of reversionary assets.

The resulting operating loss was due to the continued planned increase in overheads due to substantial investment in people and systems to enable the Bank to deliver on its growth aspirations over the coming years. The Bank continues to make significant investment, particularly on automating key operating platforms and in first and second line risk and compliance activities, recognising that any successful financial services business must invest to stay relevant and to meet the aspirations and expectations of its customers.

The Board made the decision to sell its last remaining portfolio of equity release mortgages during the year, generating a loss of £5.5 million. The disposal of this portfolio significantly reduces the Bank's susceptibility to both house price and interest rate risk.

These risks will be further reduced following the planned disposal of the Reversion portfolio in Q1 of FY22.

Other fair value gains of £11.3 million results, driven by an increase in the house price index and an increase in interest rates, results in an overall profit before tax of £3.7 million.

Our Shareholder's funds were further improved due to a £6.8m positive movement in the defined benefit pension scheme.

Chief Financial Officer's Statement (continued)

Balance Sheet overview

	2021 £m	2020 £m	% Change
Liquid assets[1]	530.2	352.4	50.5
Loans and advances to customers	1,061.5	930.8	14.0
Investment properties	94.6	97.4	(2.9)
Other assets[2]	27.1	28.6	(5.2)
Total assets	**1,713.4**	**1,409.2**	**21.6**
Deposits from banks	145.0	87.5	65.7
Deposits from customers	1,381.0	1,071.4	28.9
Other liabilities[3]	24.6	88.3	(72.1)
Pension liabilities	14.2	21.0	(32.4)
Share capital and reserves	148.6	141.0	5.4
Total liabilities and equity	**1,713.4**	**1,409.2**	**21.6**

1 Liquid assets: made up of Cash and balances held at central bank, Government bonds, Debt securities and Loans and advances to credit institutions
2 Other assets: made up of Intangible assets, Property plant and equipment, Deferred tax assets and Other assets
3 Other liabilities: made up of Derivative financial instruments, Other liabilities

Loans and advances to customers
The Bank continues to focus on its core markets of residential and commercial mortgages. The net lending figure has been driven by record gross lending of residential mortgages which has been offset by redemptions and the successful exit of a number of legacy commercial lending exposures and the disposal of the equity release mortgage portfolio.

Liquidity
The Bank holds liquid assets to meet its financial obligations in both business-as-usual and stressed situations. As at the year-end, the Bank held £530.2 million of liquid assets (2020: £352.5 million) which are available to protect it from liquidity stresses.

Liquidity levels continued to be within board risk appetite and regulatory requirements throughout the period.

This includes the Liquidity Coverage Ratio ('LCR'), which ensures that sufficient high-quality liquid assets are held to survive a short term severe but plausible liquidity stress. The Bank's LCR as at 30 September 2021 was above the regulatory minimum of 100% at 349.6% (2020: 272.9 %), this being driven mainly by the increase in liquid assets.

Funding
Retail savings remain a primary funding source and we have focused on enhancing the services we provide to customers. At the year-end savings balances were £1,381.0 million (2020: £1,071.4 million).

Defined benefit pension scheme
During the year, the Bank closed its defined benefit pension scheme to further accrual, which was available to all employees and replaced with a defined contribution scheme. At 30 September 2021, the defined benefit scheme had a deficit (the difference between scheme assets and scheme liabilities) of £14.2m (2020: £21.0m). The Group made contributions to the scheme of £5.3 million in 2021 which included an additional £4.0m deficit payment (2020: £1.6m). The scheme also benefited from £2.6m of actuarial gains, primarily due to the rise in interest rates.

Chief Financial Officer's Statement (continued)

Capital and Leverage
The Bank holds capital to protect itself, and depositors against unexpected losses. The amount of capital required to be held is determined as part of the Bank's capital risk appetite which assesses the material risks to which the Bank is exposed, how those risks are managed and the level of capital to be held against them.

The Bank's primary measure for assessing capital adequacy is the Common Equity Tier 1 ratio ('CET1'). This ratio assesses the amount of the highest quality of capital as a proportion of risk weighted assets. The Bank uses standardised risk weights to calculate the risk weighted exposure. As at 30 September 2021 the Bank's CET1 ratio stood at 20.2% (2020: 19.7%).

Alongside the CET1 ratio we actively monitor our Leverage ratio. This is a capital ratio that excludes the risk weighting of assets. The Leverage ratio at 30 September 2021 was 8.3% (2020: 9.6%). At present, we are not captured under the Financial Policy Committee's Leverage Ratio Framework. However, the leverage ratio will become a binding requirement in 2022, albeit the Bank comfortably meets the requirements.

Jan Preece
Chief Financial Officer
6 December 2021

Long-term Viability Statement

Hodge assessment of prospects

The resilience of our business model is relevant to any consideration of our prospects and viability. We benefit from the diversification between our specialist mortgages and our commercial lending businesses, which enables our services to be provided in a capital-effective way allied with our track record in attracting funding from different sources. We assess our prospects on a regular basis through our financial planning process. Our rolling five-year strategy forecasts the Bank's profitability, cash flows, capital and funding requirements and is reviewed by the Board each year.

Our business and financial planning also takes into account our obligations to depositors and the funding of our defined benefit pension scheme.

The Board believes that the market for our products will be strong for at least the next ten years, this is supported by the increasing customer demand. In addition, during the year the Bank has continued to diversify with the launch of capital repayment mortgage products.

Our commercial lending proposition is dependent on meeting the individual needs of our customers, tailoring our approach to accommodate their specific set of circumstances. The digitalisation of our savings business will assist in making Hodge less dependent on its existing customer base and our commitment to ensuring that customers can deal with us through their channel of choice means that the directors are confident that the Bank will continue to retain and attract loyal depositors. Given the long-term nature of many of the businesses mortgage products, the directors have also given due regard to the possible impact of climate change on its future prospects.

Impact of COVID-19

The longer-term impact of COVID-19 is still uncertain. There has been a partial economic recovery in 2021 and the housing market in particular has proven buoyant. However, the wind-down of the furlough scheme and possible reduction in other Government support means that there remains some caution over the wider economy. At the date of signing the financial statements, there remains a range of outcomes in relation to COVID-19.

Hodge response

The Bank continues to track its own metrics, political developments and discussions on these matters are commonplace in committees and the Board, particularly given the material uncertainty and its impact on economic fundamentals. The risks associated with individual topics are given considerable thought and discussion as to how they may materialise and impact the Bank's strategy, customer base and the capital and liquidity implications of these.

Consideration of risks

Consideration of the risks may be summarised as follows:

- Credit risk – analysis of the impact on mortgage affordability and house prices caused by adverse economic conditions arising. The loan book has been stressed extensively over a five-year horizon against a range of macro-economic assumptions, some severely adverse;
- IFRS 9 Stage 1 and Stage 2 provisions have been run under a variety of economic scenarios including a 100% weighting to the negative scenario to reflect the worst-case position.
- Capital – credit losses and net interest income impacts have been considered including those associated with the Bank of England's publicised scenarios; and
- Liquidity – the risks associated with adverse impacts on liquidity have been considered.

Extensive modelling and stress testing around macroeconomic outcomes from COVID-19 associated risks has determined that the business remains viable and able to meet its risk appetite limits and regulatory obligations.

Viability statement

The directors have carried out an assessment of the longer-term viability of the Bank. The assessment covers a period of five years, as this is the period covered by the Bank's rolling five-year strategy and regulatory and internal stress testing. The time period chosen reflects the consideration that the level of uncertainty relating to the assessment increases the longer the period chosen. The pace of change of the economic, market and regulatory environments in which the Bank operates may undermine the reliability of longer forecasts. The directors have based this statement on a robust assessment of those risks that could threaten the business model, future profitability, solvency, liquidity or capital adequacy of the Bank.

In making the assessment, the directors considered a range of information concerning each of its principal risks, individually and collectively, over a range of scenarios, including but not limited to, the Bank's rolling five-year plan and the programme of regulatory and internal stress testing it undertakes, further details of which are as follows:

- The plan is reviewed by the directors in detail at least annually. The plan makes certain assumptions about the performance of the Bank and the economic, market and regulatory environments in which it operates. The planning process is underpinned by a robust stress testing framework to ensure compliance with the Bank's risk appetite.
- Alternative forecasts are also constructed against a number of stress scenarios, including a robust downside scenario as part of the Board's review of Hodge Bank's

Long-term Viability Statement (continued)

ICAAP. This involves considering a severe stress to the UK economy, with a significant fall in both residential property prices and secondary commercial real estate values and low interest rates for a sustained period. The results of the ICAAP are submitted to and discussed with the PRA.

- Liquidity stress tests are conducted as part of the Bank's ILAAP. The ILAAP demonstrates that the Bank holds sufficient liquid assets to meet cash outflows during a severe-but-plausible scenario where there is a combined, market-wide and firm specific stress.
- The review also considered all aspects of emerging regulation where there is sufficient clarity to inform the analysis. For example, the assessment of the Bank's capital position reflects the latest understanding of the capital buffer and leverage requirements likely to be imposed on the Bank.

Based on this assessment, the directors confirm that they have a reasonable expectation that the Bank will be able to continue in operation and meet its liabilities as they fall due during the period to 30 September 2026.

Graeme Hughes
Chairman
6 December 2021

Corporate Governance

Corporate Governance

A comprehensive corporate governance framework is vital in supporting executive management in its execution of strategy and in driving long-term sustainable performance. It helps ensure that the Shareholder's investment in Hodge is protected, while at the same time recognising the interests of our wider stakeholders.

The Bank's approach to corporate governance is based on the Principles and Provisions of the UK Corporate Governance Code. Although the UK Corporate Governance Code is primarily aimed at listed companies, the Bank's Board is committed to operating in line with best practice standards of corporate governance. For this reason, the Board chooses to comply with the UK Corporate Governance Code in so far as is relevant to private financial services companies.

The Board's agenda during FY 2021 was focused on overseeing and supporting executive management to deliver on Hodge's strategic objectives. It is during periods of significant change, which Hodge is currently undergoing, that leadership and good governance are more important than ever.

The Board comprises of three executive and five non-executive directors. The roles of Chairman and Chief Executive are separate to ensure that neither can exercise unfettered powers of decision-making on matters of material importance.

The Board has sought to ensure that directors are properly briefed on issues arising at board meetings by:

- Distributing papers sufficiently in advance of meetings;
- Considering the adequacy of the information provided before making decisions; and
- Deferring decisions when directors have concerns about the quality of information.

The Board is ultimately responsible for the Bank's system of internal control and for reviewing its effectiveness. The system of control is designed to manage rather than eliminate risks which are inherent in the Bank's business and can provide only reasonable and not absolute assurance against material misstatement or loss.

The Bank's system of internal financial control includes appropriate levels of authorisation, segregation of duties and limits for each aspect of the business. There are established procedures and information systems for regular budgeting and reporting of financial information. Financial reports are presented at every board meeting detailing the results and other performance data.

The Group outsources its internal audit function to Deloitte. The primary purpose of this function is to review the effectiveness of controls and procedures established to manage risk. An audit programme is agreed annually in advance with the Audit Committee and the Head of Internal Audit attends each meeting to present a summary of audit reports completed during the period and to provide any explanations required by the Committee.

Governance framework

With the sale of Hodge Life to a third party by the Bank's parent, Hodge Limited, a key focus has been simplifying and strengthening the governance framework to support the ambitious growth plans of the Bank in the coming years.

COVID-19

The impact of COVID-19 continued to be a key area of focus during the year, with the Board continuously reviewing our response to the pandemic throughout our business and governance, protecting the health and well-being of our colleagues as well as maintaining the financial and operational integrity of the Bank.

The Board

The Board has ultimate responsibility for the proper stewardship of the Bank in all its undertakings. It meets regularly throughout the year to discharge its responsibilities for all important aspects of the Bank's affairs, including monitoring performance, considering major strategic issues, approving budgets and business plans and reviewing operational performance. The Board holds regular discussions with the Bank's shareholder to ensure a clear understanding of their views and requirements. A shareholder's covenant has been agreed detailing the Shareholder's expectations of the Bank.

The Chair is responsible for the leadership and operation of the Board, setting the agenda and the tone of board discussions as well as having responsibility for assessing the effectiveness of the Board and its directors.

A board control manual has been adopted and was updated during the year which describes the high-level policy and decision-making arrangements within the Bank. The manual includes a schedule of matters reserved to the Board together with those items delegated to directors and board and executive committees.

Details of the members of the Board are set out below.

Graeme Hughes – Chair

Graeme joined the Board in 2019 and was appointed Chair in May 2020. Graeme has spent the vast majority of his career with the Nationwide Building Society, most recently becoming its Group Distribution Director, responsible for all sales and service activities across 720 branches and 10,000 staff. Earlier roles have seen him leading group strategy and planning, as well as human resources and external affairs.

Corporate Governance (continued)

John Barbour – Non-Executive Director

John joined the Board in March 2017 and is also Chair of the Audit Committee. John was previously Managing Director of Treasury at ICBC Standard Bank, the London-based financial markets and commodities bank, owned by China-based ICBC and South African-based Standard Bank. He has spent his entire career in treasury and financial markets-related roles, having previously worked at Investec and the Bank of New York.

Helen Molyneux – Non-Executive Director

Helen joined the Board in June 2015 and is the Chair of the Remuneration Committee.

Until November 2016, Helen was the CEO of New Law Legal, a business she established from scratch, which now employs over 400 people. She is also a non-executive director of the EUI board of the Admiral Insurance Group.

In 2011, Helen was named Welsh Woman of the Year and in 2013 the Law Society's Business Woman of the Year. She was a member of the Silk Commission on Devolution in Wales and was previously chair of the Institute of Welsh Affairs. In 2016 she was awarded an honorary doctorate by the University of South Wales in recognition of her services to the legal profession.

Aileen Wallace – Non-Executive Director

Aileen joined the Board in April 2020 and is Chair of the Innovation and Change Committee. She is an experienced executive turned advisor and non-executive director with more than 30 years' experience in senior financial services and digital services roles at Virgin Money (formerly CYBG Plc), Co-operative Bank, Cognizant and pre-seed Fintech. A Chartered Banker, her expertise is in business transformation, technology and customer innovation and corporate governance in highly regulated environments. Aileen is currently a non-executive director at Target Group.

Iain Laing – Non-Executive Director

Iain joined the Board in July 2020, and is the Chair of the Risk and Conduct Committee. He is also Chief Risk Officer of Monzo. Prior to joining Monzo, Iain had been Chief Risk Officer and a member of the executive committees of TSB Bank and Nationwide Building Society, and was Chief Credit Officer of Santander UK Retail throughout the 2007 to 2010 financial crisis.

David Landen – Chief Executive Officer

David was appointed Chief Executive Officer (CEO) in September 2020, stepping up from Chief Financial Officer (CFO) and Deputy CEO. David joined the Group in 2002 and has held a variety of finance and treasury roles during his time with the organisation. He was appointed to the Board as CFO in 2011. An accountancy graduate from Cardiff University, he is a fellow of the Association of Chartered Certified Accountants.

Matthew Burton – Retail Director and Deputy Chief Executive Officer

Matthew joined the Board in April 2020 on his appointment as Interim CFO. He has since been appointed as Group Retail Director and Deputy Chief CEO. Matthew joined Hodge in 2015 as the Group's Head of Finance, before taking up the role of Managing Director of Mortgages in February 2019. Matthew has a 14-year career in finance – having held roles at Future plc, Zodiac Aerospace and BDO LLP.

Janet Preece – Chief Financial Officer

Janet joined the Hodge Group and was appointed CFO in September 2021. Janet has a 25-year career in finance having previously performed the Finance Director role for Friends Provident International (part of the Aviva Group) and prior to that several senior finance roles, including Finance Director within the General Insurance Business of Lloyds Banking Group.

Board Committees

The Board has established the following standing committees:

Audit Committee:

John Barbour (Chair), Helen Molyneux, Alun Bowen (to 31/12/2020), Aileen Wallace, Iain Laing, David Gulland (to 30/06/2021) and Alison Halsey (from 06/11/2020 to 31/08/2021).

All members of the Audit Committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chair.

The function of the Audit Committee is to review the work of the internal audit function, to consider the adequacy of internal control systems, to oversee the relationship with the external auditors, to review the statutory accounts including the key estimates and judgements use d in the statutory accounts and to consider compliance issues.

The Committee meets at least four times a year. A report from the Chair of the Audit Committee can be found on page 42.

Risk and Conduct Committee:

Iain Laing (Chair), Alun Bowen (to 31/12/2020), Graeme Hughes, John Barbour, Helen Molyneux, Aileen Wallace and Alison Halsey (from 06/11/2020 to 31/08/2021).

All members of the Risk and Conduct Committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chair.

The function of the Risk and Conduct Committee is to oversee the management of risk and the conduct of business on behalf of the Board to ensure that significant risks are identified, understood, assessed and managed and that good customer outcomes are achieved. It is responsible for the second line of defence of the business, ensuring that the level of assurance available to the Board is sufficient and appropriate.

Corporate Governance (continued)

The Committee meets at least eight times a year. A report from the Chair of the Risk and Conduct Committee can be found on page 46.

Nomination and Governance Committee:

Graeme Hughes (Chair), Helen Molyneux, John Barbour, Aileen Wallace and Alison Halsey (from 06/11/2020 to 31/08/2021).

All members of the Nomination and Governance Committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chair.

The function of the Committee is to recommend the appointment of directors to the Board and board committees and to ensure that the Bank has an appropriate succession plan for executive and senior management positions. It also is responsible for ensuring that the Bank's Diversity and Inclusion policy is being delivered.

The Committee meets at least 4 times per year. A report from the Chair of the Nomination and Governance Committee can be found on page 50.

Remuneration Committee:

Helen Molyneux (Chair), Graeme Hughes, Aileen Wallace, Iain Laing, David Gulland (to 30/06/2021), Alison Halsey (from 06/11/2020 to 31/08/2021).

All members of the Remuneration Committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chair.

The function of the Remuneration Committee is to consider remuneration policy and specifically to determine the remuneration and other terms of service of executive directors and senior managers. The executive directors decide fees payable to non-executive directors.

The Committee meets at least 4 times per year. A report from the Chair of the Remuneration Committee can be found on page 52.

Innovation and Change Committee:

Aileen Wallace (Chair), Helen Molyneux, David Gulland (to 30/06/2021) Graeme Hughes (from 21/07/2021) and Alison Halsey (from 21/07/2021 to 31/08/2021).

All members of the Innovation and Change Committee are non-executive. Executive members of the Board and other senior executives attend as required by the Chair.

The function of the Committee is to oversee the end-to-end digital delivery of the Bank's product and services. It monitors investment and management of risk associated with the delivery of change associated with the Bank's strategic initiatives.

The Committee meets at least 4 times per year. A report from Innovation and Change Committee can be found on page 54.

Corporate Governance (continued)

Name	Board		Audit Committee		Risk and Conduct Committee		Nomination and Governance Committee		Remuneration Committee		Innovation and Change Committee	
	(a)	**(b)**	**(a)**	**(b)**	**(a)**	**(b)**	**(a)**	**(b)**	**(a)**	**(b)**	**(a)**	**(b)**
Graeme Hughes	15	15	-	-	9	9	5	5	8	8	1	1
John Barbour	15	15	6	6	9	9	5	5	-	-	-	-
Helen Molyneux	15	15	6	5	9	8	5	3	8	8	4	4
Alun Bowen	3	3	3	3	2	2	-	-	-	-	-	-
Aileen Wallace	15	15	6	6	9	9	5	5	2	2	4	4
Iain Laing	15	15	6	6	9	9	-	-	2	2	-	-
Alison Halsey	10	9	3	3	8	7	3	3	6	6	1	1
David Gulland	-	-	5	5	-	-	-	-	7	7	3	3
David Landen	15	15	-	-	-	-	-	-	-	-	-	-
Matthew Burton	15	15	-	-	-	-	-	-	-	-	-	-
Richard Jones	12	12	-	-	-	-	-	-	-	-	-	-
Janet Preece	1	1	-	-	-	-	-	-	-	-	-	-

(a) Number of meetings held **(b)** Number of meetings attended

Notes
Alun Bowen resigned from the Board on 31/12/2020.
David Gulland resigned from the Audit Committee, Remuneration Committee and Innovation and Change Committee on 30/06/2021.
Alison Halsey joined the Board on 06/11/2020 resigned from the Board on 31/08/2021.
Richard Jones joined the Board on 09/10/2020 and resigned from the Board on 03/09/2021.
Janet Preece joined the Board on 30/09/2021.

Risk Management

As a financial services provider in the UK managing risk effectively is fundamental to our strategy, long term resilience and to operating successfully day to day. This is supported by a business model with a medium to low risk profile which over the past year has seen a number of initiatives to reduce volatility of some key risks by removing elements of exposure not easily mitigated through management actions.

Over the past year, the COVID-19 pandemic has persisted and whilst the business impacts and disruption have been managed and the economic impact, so far, less than initially suggested the ongoing uncertainty remains as the government support measures are withdrawn, but there are positive signs emerging and therefore the Bank is taking cautious steps whilst seeking to fulfil its strategy.

Risk Management Framework

The Bank's Risk Management Framework is an integral part of the Hodge business model to support:

- Delivering against its strategy within an appropriate risk culture;
- Building greater resilience to organisational threats;
- Protecting its customers from unfair outcomes.

The Bank's strategy and business model is underpinned by clearly defined risk governance, ensuring alignment with the Board's appetite for risk. Hodge operates entirely within the UK financial services market and only takes on risks, which it has the capability to understand and manage effectively. A Risk Management Framework, supported by a three lines of defence governance model, ensures strong risk awareness, assessment, monitoring and management across all principal and emerging risks. Risks are managed within the risk appetite set by the Board and stress testing is undertaken to ensure that the capital and liquidity of the Bank would enable it to survive severe but plausible market-wide and firm specific stresses.

Our Risk Management Framework sets out how we manage and control risk and during 2020/21 this was reviewed, resulting in simplifying our risk hierarchy and risk appetite and also redefining the Risk Management Frameworks for each of these principal risks. As part of these reviews, Climate Change has been added as a risk category to ensure focus is maintained but acknowledging that it is a transversal risk with impacts occurring across all other risk types.

The improvements to risk management through ongoing refinement of policies, processes and procedures, and recruitment of risk resources across both first and second lines of defence will further embed and mature the risk management capabilities through 2022.

Risk Culture

Hodge has a strong culture of risk awareness and control and actively monitors and manages the risks of its business, as well as emerging industry risks which may have an impact on those activities, through its Risk Management Framework.

This culture is embedded through clear expectations of roles and responsibilities and supported by defined risk appetite and risk management policies, together with effective training for all levels of staff. The Board supports a culture of openness and transparency, encouraging issues to be raised as identified and providing the necessary resources and support to remediate. This is underpinned by an emphasis on good customer outcomes and sustainability of the business.

Risk Management (continued)

Three Lines of Defence Model

The Bank operates a three lines of defence model which clearly sets out responsibilities for the management and oversight of risk. The Board retains ultimate responsibility for risk management. The three lines of defence model is summarised below:

First Line of Defence – Day-to-Day Risk Management

The first line of defence has responsibility for implementation of the Bank's strategy and for the management of risk across the organisation and is comprised of executive committees, management and staff.

Second Line of Defence – Risk Oversight

The second line of defence is responsible for providing independent oversight and challenge of activities undertaken by the first line and provides guidance on risks relevant to the strategy. This is provided through the Risk & Compliance function, which is led by the Chief Risk Officer ('CRO') who reports to the CEO and has an independent reporting line to the Chairman of the Risk and Conduct Committee. It maintains and reports an aggregate view of risks and performance in relation to risk appetite to the Risk and Conduct Committee. The Risk function is not customer facing and has no responsibility for business targets or performance.

Third Line of Defence – Internal Audit

The third line of defence provides objective assurance on the design and effectiveness of the Bank's governance, and activities of the first line and second line of defence. This assurance is obtained through the use of internal audit services provided by Deloitte. Internal audit reports directly to the Chair of the Audit Committees and the CEO and is independent of the first and second lines of defence.

Risk Management (continued)

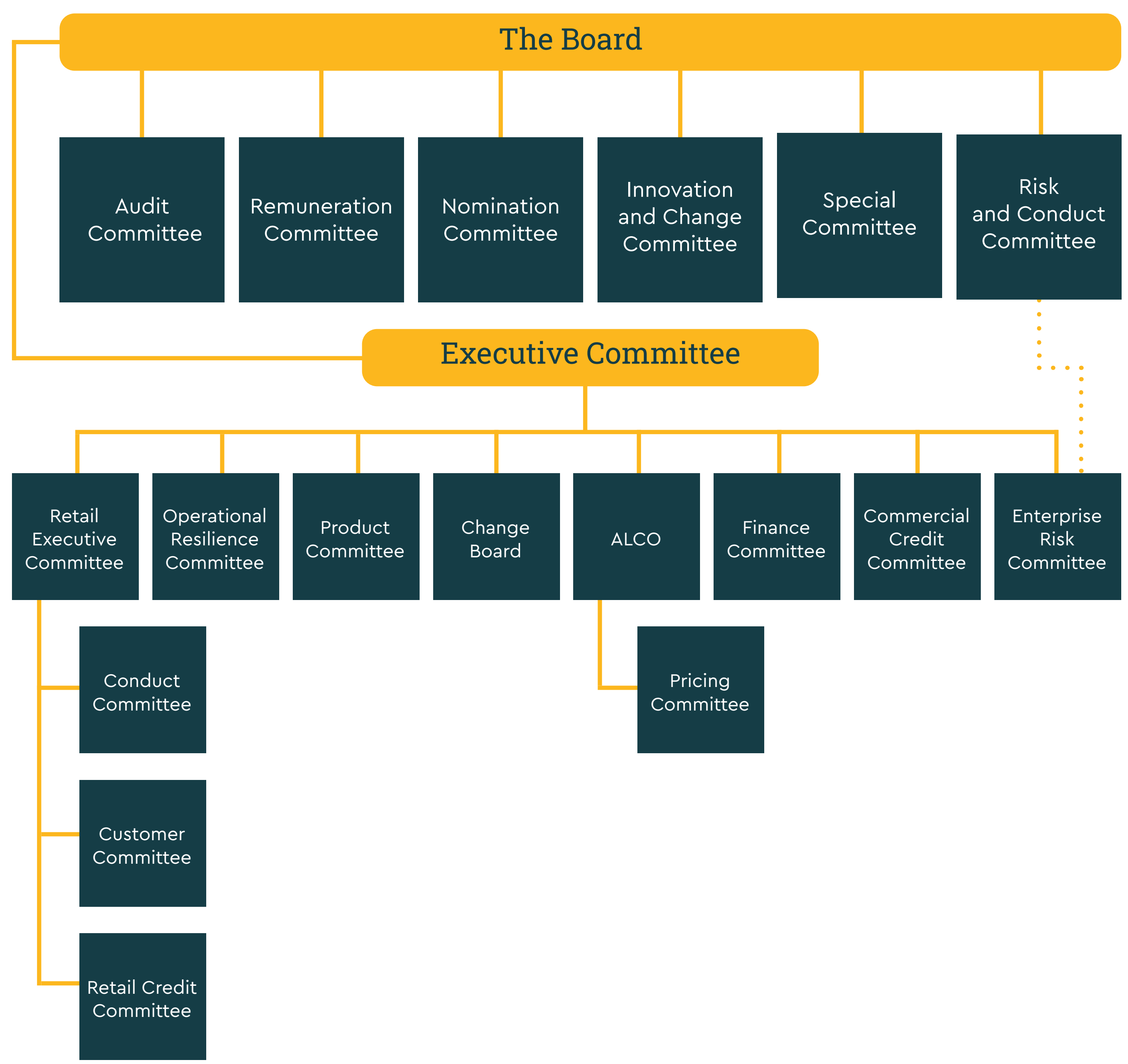
Risk Governance Structure

The Board is ultimately responsible for the overall risk governance and effective management of risk within the Bank. The Board determines the risk strategy and ensures that risk is monitored and controlled effectively.

The Risk and Conduct Committee is a board committee that reviews, on behalf of the Board, the key risks inherent in the business and the control framework in place to manage such risks, reporting its findings to the Board.

There is a formal structure of Risk Management Frameworks and policies in place, setting out risk limits and triggers and minimum operating standards, which are aligned to the Board's risk appetite.

Risk governance is supported by a structure comprising of executive committees, each with escalation routes for risk matters through the Risk and Conduct Committee and Board as shown below:



Executive Committees:

Each committee includes appropriate representation from the Executive Committee and risk specialists. The responsibilities of each of the Committees is documented in the Terms of Reference of that committee, a high-level summary is set out below:

Enterprise Risk Committee is chaired by the Chief Risk Officer. The Committee is responsible for oversight and monitoring of all enterprise wide risks and for the development of the Risk Management Framework.

Operational Resilience Committee is chaired by the Chief Technology Officer. The Committee's purpose is to provide operational resilience governance across the firm. This governance covers a range of key activities inclusive of oversight of internal and outsourced operations, operational resilience and forward-looking operational impacts to the business.

Conduct Committee is chaired by the Retail Director. The Committee is responsible for the identification, management and monitoring of the conduct risk across the business and to assist in the development and implementation of the Conduct Risk Framework and ensuring adequacy of the control environment.

Change Board is chaired by the Chief Technology Officer. The purpose of the Change Board is to ensure the Bank's Change Programme is aligned with its strategy and business plans and to monitor programme delivery, budget and resources.

Product Committee is chaired by the Retail Director. The purpose of the Committee is to challenge and approve new product proposals and to regularly monitor existing and legacy products to ensure they are performing in line with the standards and expectations on which they were approved.

Assets & Liabilities Committee ('ALCO') is chaired by the Chief Financial Officer. The Committee is responsible for the management of and implementation and maintenance of policies relating to capital management, liquidity management, interest rate risk and treasury credit risk.

Retail Credit Risk Committee is chaired by the Retail Director. The Committee is responsible for the implementation and maintenance of Retail Credit Risk policy. The scope of the Committee covers monitoring and development of all retail lending activity.

Commercial Credit Risk Committee is chaired by the Managing Director of Commercial Lending. The Committee is responsible for the implementation and maintenance of Commercial Credit Risk policy. It is also responsible for reviewing, challenging and if appropriate, approving credit proposals for new commercial lending deals within its delegated authority.

Finance Committee is chaired by the Chief Financial Officer and it reviews and challenge the application and changes to significant accounting policies within its delegated authority. It also ensure that appropriate estimates and judgements are used in the Bank's accounting policies.

Risk Strategy

The Bank's risk strategy sets out the risk management approach to support the achievement of its strategic ambitions. It sets out which risks will be avoided, mitigated or accepted and is implemented by defining tolerances to the risks it faces through its risk appetite.

The strategic risk management objectives are to:

- Identify, assess and monitor the risks arising from the business model.
- Set appropriate risk appetite with defined measures and limits.
- Ensure appropriate skills and resources are present for effective management of risks.
- Identify and track treatment plans for known control weaknesses.
- Scan the horizon for emerging risks and regulatory changes.

Risk Appetite

The Board sets a risk appetite to define the level of risk that the Bank is willing to accept or wishes to avoid in order to meet its business objectives. A risk appetite statement is in place that includes both qualitative statements and quantitative measures and addresses each of the key risk types faced by the Bank as articulated within the Risk Strategy.

The risk appetite statements are linked to the Bank's strategy and supported by a suite of risk metrics, limits and triggers designed to monitor its exposure to the principal risks and together outline parameters within which the Bank operates.

The risk appetite statement provides a framework against which all business decision making must be assessed.

Top and Emerging Risks

In addition to the principal risk categories noted below, the Bank's top and emerging risks are identified through the Bank's risk management processes. These are specific risks within the Bank's principal risk categories that are significant to the Bank throughout its strategic plan. The key risks and details of how they are mitigated is set out below:

Current threat / Emerging risk	Mitigation / Strategic response
Pandemic Risk/COVID The continuing global pandemic due to COVID has, and continues to, cause disruption to global economies and populations. Although considered to be a receding risk compared to its peak, the tail risks and impacts are still prominent on the agenda.	The Bank responded to COVID-19 as it developed, initially through its business continuity processes to ensure the safety of its colleagues and its customers before returning to a more 'business as usual' operation albeit operating remotely. The Executive Committee meets regularly to identify issues and actions to remediate. Hodge has responded to and follows government guidance and best practice to maintain our customer service levels and protect our employees. Hodge provided temporary payment holidays through the pandemic for which the majority have been repaid with the remaining taking longer term forbearance. Stress testing was undertaken aligned to the external economic scenarios published. Economic developments are regularly discussed in governance forums and monitored closely. Lessons learned from our progress through this pandemic have led to improvements in the firm's operational resilience processes.
Market/competitive environment COVID has changed customers behaviours and requirements which has the potential to change their financial service requirements. It has also led to economic uncertainty. Disruptive technologies, new competitors (traditional and non-traditional) and a search for yield all have the ability to threaten the current business model and achievement of the strategy.	Continual monitoring of customer needs and the competitive environment is undertaken and discussed regularly alongside strategy development. Competitor benchmarking and networking forums allow insight into firm's potential strategic intent. Appropriate market research and product development governance processes are conducted to ensure strategic initiatives are properly controlled. Strategic initiatives have been completed to simplify the business model and exit assets that can cause significant volatility to the results. As the UK experienced a downturn following COVID, Hodge took action to tighten its credit policies to protect the balance sheet during this time.
Change & execution risk The Bank has committed to a number of strategic change initiatives which are key to the achievement of our strategic objectives. These significant activities increase cost and execution risk including timelines for delivery.	The change programme will deliver additional resilience to the Bank's business model and its operational resilience once fully implemented. Several of the change initiatives completed in the reporting period have been focused on simplifying the business model to improve resilience. The change programme has risk management processes in place to ensure safe and controlled delivery of the initiatives required. Retrospective reviews of change delivery are regularly carried out to continually learn from the process.

Continued

Top and Emerging Risks (continued)

Current threat / Emerging risk	Mitigation / Strategic response
Cyber threat The threat of cyber related attacks remains prevalent across all industries. The sophistication of the attacks continues to improve and the threat of not maintaining and improving the security of the organisation has the potential to lead to vulnerabilities. Key threats include: • compromised customer accounts; • security vulnerabilities; • ransomware attacks; • attacks on third parties.	Hodge continues to review and invest in its cyber security control environment to reflect the ever-changing nature of cyber threats. It also protects itself against the impact of this risk by holding cyber risk insurance. Recruitment of additional resource in the Cyber Risk team to strengthen the skills and capabilities of the organisation. Test scenarios have been conducted to assist in the identification of potential vulnerabilities with actions to remediate and address any weaknesses identified.
Climate Change risk Climate change continues its rise up the agendas of businesses and understanding. Financial risks from climate change arise through two primary channels; physical i.e. specific weather events and damage to assets and transition risks i.e. increased regulation to adjust to low carbon economy.	ESG considerations are taking greater prominence in the strategic plan and risk agendas, particularly climate change risk and as such a fast-moving topic it is offering risks and opportunities which require consideration for achievement of both firm level and global targets on climate change. The business has a clear plan to achieve compliance with the regulatory requirements under SS3/19 which is on track. The Chief Risk Officer has been charged with ensuring consideration of transitional risks (including legal and regulatory risks) arising from climate change and embedding this in the Risk Management Framework. Climate change risk has been added to the risk taxonomy across the organisation. The financial risks from Climate change are being addressed specifically as part of the ICAAP but also the knowledge learnt is then informing strategic and business model decisions.

The Bank conducts on-going horizon scanning to identify new risks that could threaten achievement of the strategy and ensure they are captured in the Risk Management Framework as early as possible. The governance structure in place enables a strong awareness of current and emerging risks, which are recorded and monitored to ensure that appropriate mitigation and monitoring strategies are adopted. Mitigating actions are logged, business owners allocated, and warning indicators identified to ensure effective ongoing monitoring. Oversight of emerging risks is provided by the Risk and Conduct Committee.

Principal Risks

These are the most significant risks faced by Hodge which could impact the viability of the Bank and delivery of our strategic objectives. Risk appetite limits and triggers as well as key risk indicators are in place for each principal risk and reported to the relevant executive committee. Aggregated reporting is provided to the Risk and Conduct Committee to support it in its duties. During 2021 the principal risks have been slightly revised from last year to support better flow and escalation of risk for the business.

CREDIT RISK – the risk that a counterparty will be unable or unwilling to meet a commitment that it has entered into with the Group when it falls due.

Key drivers and appetite	Our approach
Credit risk emerges from commercial lending exposures, residential mortgages to retail customers and from investments held by the Treasury function. Concentration risks within and across these portfolios is also considered. The Bank is willing to be exposed to a moderate level of risk for an acceptable return.	The Bank assesses its exposure to and management of credit risk with reference to three sub-categories: • **Retail credit risk** – the risk of financial loss from residential mortgages due to the customer's failure to service interest or repay capital. • **Commercial credit risk** – the risk of financial loss from a commercial lending customer's failure to settle financial obligations as they fall due or movements in commercial real estate prices. • **Treasury credit risk** – the risk that a debt issuer or counterparty will fail to make payments (either interest or principal) in a timely manner or the credit worthiness of borrowers deteriorate reducing the value of investments. Within each business line there is dedicated first line risk management provided by appropriately skilled credit managers and treasury staff. Pricing of lending products includes a component of margin to cover expected credit losses. Treasury counterparties are restricted to a number of well-established and externally rated institutions. The following mitigation practices are in operation: • Approved underwriting policies and authorisation mandates are in place for each sub-category in order to direct lending decisions, ensuring that the Bank lends responsibly while taking an acceptable level of credit risk. • Rating and scoring systems in place and controls to support lending decisions with the addition of affordability stress tests. • Limitations on concentration risk across portfolios are implemented via risk appetite limits on large exposures, geographical and sectoral exposures, and loan to income ratios. • Appropriately skilled colleagues are employed by the Bank to monitor and manage credit risk within the defined parameters set by the Board. • Portfolio level stress testing and scenario analysis.

Principal Risks (continued)

FINANCIAL RESILIENCE RISK – the risk that the Bank fails to maintain or protect its capital and liquidity resources to meet regulatory requirements, absorb volatility and losses through economic cycles and changes in market rates, and to maintain the confidence of customers, investors and regulators.

Key drivers and appetite

Financial resilience risk arises from changes to the respective resources (i.e. capital, liquidity) and risk profiles of the Balance Sheet driven by customer behaviour or management decisions. It also arises from the external environment, including changes to market metrics such as interest rates or property prices together with changes to the regulatory regime.

The Bank aims to mitigate financial resilience risk where possible and commercially viable to do so and any residual risks have financial resources allocated to support them.

Our approach

The Bank assesses its exposure to and management of Financial resilience risk with reference to the following sub-categories:

- **Capital risk** – the risk that the Bank fails to maintain sufficient capital to meet regulatory requirements, absorb volatility and losses through economic cycles, and to maintain the confidence of customers, investors and regulators.
- **Liquidity risk** – the risk that the Bank is unable to meet its financial obligations as they fall due or unable to maintain customer and stakeholder confidence or can only do so at an uneconomic cost.
- **Interest rate risk** – the risk of loss in the value of, or net income arising from, assets and liabilities due to changes in the market level of interest rates.
- **Market risk** – the risk that the net value of, or net income arising from, assets and liabilities is impacted because of market price or rate changes.

Treasury and Finance provide strong first line risk management expertise and have day to day responsibility for the management of financial resilience risk within defined board policies and limits. The following mitigation techniques are in operation:

- Frequent monitoring and reporting of exposures, portfolio composition and changes and forecasts of key ratios.
- Reporting of regulatory key metrics across capital, liquidity and interest rate risk.
- Stress tests run to ensure the Bank maintains adequate levels of capital and liquidity for business purposes even under stress.
- Well defined board policies and limits, monitored regularly.
- Extensive contingency and recovery plans in place.
- Key regulatory assessment documents embedded for ICAAP, ILAAP and Recovery Plan.
- Maintenance of high-quality capital surplus.
- Maintenance of a liquidity buffer of high-quality liquid assets.
- Well matched maturity profile of assets and liabilities.
- Composition, credit quality and maturity profile of liquidity portfolio and funding balances in line with agreed policies.
- The interest rate structure of assets is matched with liabilities to create a natural hedge and supported by derivatives where appropriate.
- Various interest rate stress tests are applied to the portfolio to help identify any potential weaknesses that require further remediation.

Principal Risks (continued)

STRATEGIC RISK – the risk of significant loss or damage arising from business decisions made in setting and executing the Bank's strategic plan, and/or from an inability to adapt to external developments.	
Key drivers and appetite	**Our approach**
Strategic risk can arise from changes to the business model and also the risk of the business model or strategy proving inappropriate due to macroeconomic, political, regulatory or other impacts. The risk to delivery of the strategy is deemed to be the principal risk. This category includes the risks from climate change due to impact across all risk categories.	Close management and monitoring of the strategic plan along with in-depth stress testing reported regularly through the Bank's committee structure to the Board and senior management. This is supported through additional risk reporting and monitoring of the key threats to the business on risk registers and horizon scanning to ensure the business can respond appropriately.

CONDUCT RISK – the risk that the Bank's behaviour will result in poor/unfair outcomes for customers.	
Key drivers and appetite	**Our approach**
Conduct risk is inherent in any business that provides products or services to customers. Failing to treat customers fairly and deliver good outcomes would have a detrimental impact on the success and sustainability of the Bank. The Bank assesses its exposure to and management of conduct risk with reference to four sub-categories: Product design, Distribution and sales, Product servicing, and Culture and governance.	• **Product design** – a product governance policy is in place to ensure that all new products are subject to an appropriate level of scrutiny and that existing products are subject to regular review to identify any risk of poor customer outcome. The Product Committee oversees the new product launches and annual product reviews to ensure product remains suitable for their respective target markets. • **Distribution and sales** – all customer lending products are distributed via independent brokers to ensure that customers receive independent advice. Deposits and commercial lending products are offered on an execution-only basis. Approval processes are in place to ensure that product literature is clear, fair and not misleading and complies with relevant regulation and legislation. Oversight on distribution and sales is provided by the Conduct Committee. • **Product servicing** – performance against service levels is monitored and customer feedback used to determine whether good outcomes are achieved. Internal quality assurance is undertaken. All complaints are thoroughly investigated and responded to promptly. Monitoring is in place to identify and quickly address any trends or systemic issues. • **Culture and governance** – reward strategies and incentives are not based on sales targets and mandatory conduct risk and customer outcomes training is in place for all new and existing employees.

Principal Risks (continued)

OPERATIONAL RISK – the risk of loss from control failures or external events, which result in unexpected or indirect loss to the Bank.

Key drivers and appetite	Our approach
The Bank accepts that operational risks arising from its people, processes, systems or the external environment are a natural consequence of its business operations but seeks to avoid or mitigate the risk to a minor level wherever practical. The Bank assesses its exposure to and management of operational risk with reference to nine core sub-categories: • **Process** – losses from failed transaction processing or process management. • **Data and information management** – losses due to material errors in reporting or modelling. • **Financial crime and fraud** – losses due to acts of a type intended to defraud, misappropriate property or circumvent regulations, the law or the Bank's policy. • **People** – failure to manage the human resources of the Bank in order to maximise its value. • **Legal and regulatory** – failure to comply with legal and regulatory requirements. • **Infrastructure and security** – losses or damage arising from technology through inadequate design or failure of security and resilience controls. • **Change** – failure to successfully deliver change to achieve defined strategic benefits or failure to operate robust change implementation controls resulting in disruption to operational processes and/or the customer journey. • **Third party** – services provided by third parties fail to meet required standards leading to disruption to operational processes, customer impact and/or financial loss.	Operational policies and procedures, supported by staff training, are in place to govern the way in which these risks are managed across the business. Senior management are responsible for understanding the nature and magnitude of risks within each business area, and for implementing appropriate controls to mitigate those risks. Operational losses and near-misses are recorded and analysed to determine whether there are any systemic issues that need to be addressed by the business. Horizon scanning is conducted to identify emerging regulatory and legal developments to ensure that the business can respond appropriately. This is supported by a Horizon scanning working group with representatives from across the business. Oversight on operational risk is provided by committees and governance forums. The Board is mindful that, as the digital capability of the Bank increases, the risk associated with cyber-attacks also increases. As such, particular focus continued to be given to this area throughout the year to ensure a robust cyber response.

Stress Testing and Planning

Stress testing and scenario analysis is a key tool of the Risk Management Framework which assess vulnerabilities under hypothetical or historical scenarios. The results of the stress testing identify the impact of risks that could threaten the business model, future profitability, solvency, liquidity or capital adequacy of the Bank. The Board and senior management have engaged in a number of exercises which have considered and developed stress-test scenarios covering a range of groupwide, multi-risk category stress tests, generic and idiosyncratic financial shocks, and operational and conduct risk scenario analysis in addition to the scenarios prescribed by the regulator.

Stress testing is central to the annual business planning process and to the annual review and ongoing development of the Bank's risk appetite. It is also core to the adequacy assessment processes for liquidity and capital and for assessing and improving management of the Bank's risk profile. The assessment processes for capital and liquidity are articulated through the Bank's ICAAP and ILAAP. These activities and associated documents are updated at least annually or following any significant change in the business model or risk profile.

- The ICAAP evaluates the level and quality of capital required by the Bank as defined by the Capital Requirements Directives and Regulations to ensure it adequately covers all current and future risks in the business over the medium term. In addition to the assessment these risks may pose to capital, consideration is given to the contingency actions available to the Board to mitigate those risks.
- The purpose of the ILAAP is to consider the Bank's liquidity risk management processes, an element of which is evaluating liquidity positions and requirements in both business-as-usual and stress situations. The ILAAP demonstrates that sufficient liquid assets are held to meet cash outflows during a severe but plausible scenario where there is a combined market-wide and firm-specific stress, resulting in, among other things, a significant outflow of savings accounts. The document also outlines the contingency funding arrangements available for use in a stress.

Reverse Stress Testing
The Bank also undertakes reverse stress testing which is used to explore potential vulnerabilities of the Bank's strategies and plans to extreme events that could cause the business to fail. The reverse stress tests push the severity of the stress scenario to the point at which the firm's business model becomes unviable. These exercises are designed to assess the resilience of the business to adverse competitive, economic or financial developments and ensure that robust, forward-looking capital and liquidity management processes are in place to deal with the identified risks.

The reverse stress tests complement the ICAAP and ILAAP and assist management in understanding the full continuum of the levels of stress which the business can tolerate within its current resources and risk appetite. Any plausible scenarios identified with unacceptably high risks will lead the Bank to adopt measures to prevent or mitigate those risks through a change in strategy, increased controls and early warning indicators or contingency plans.

Recovery Planning
The Bank maintains recovery plans that can be enacted in the event of internal or external triggers which threaten the liquidity or capital position of the Bank. These plans are prepared in accordance with the Bank's Recovery and Resolution Directive allowing a common approach to be taken.

The Recovery Plan describes the strategy and a 'menu of actions' that could be taken by management to allow the recovery of the Bank from a significant adverse event which would otherwise lead to failure. The Recovery Plan is informed by the outcomes of the Stress and Scenario Testing Framework which the Board and senior management use to determine the strategy and actions to support a potential recovery.

The Recovery plan outlines the processes and procedures that should be followed, along with assessing the management actions to recover from a severe but plausible financial risk event. The plan tests the early warning and invocation triggers to ensure the Bank has enough time to react and put in place recovery or mitigation actions. It has close ties to the overall business continuity plan. It is reviewed at least annually or more frequent if a material change of strategy or business model suggests.

The Resolution Plan provides data required by the PRA to be used to facilitate a rapid and orderly resolution in the event that the recovery of the Bank could not be achieved whilst maintaining any critical functions provided by the Bank to the economy.

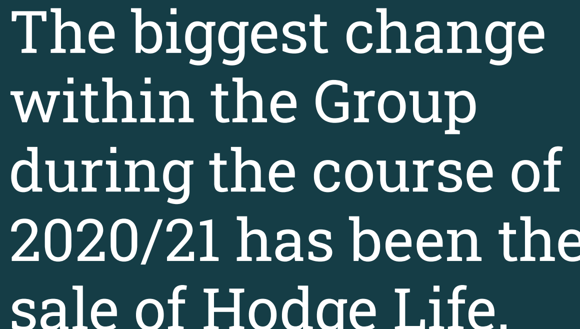
Operational Resilience
The regulatory direction provided on operational resilience through discussion and consultation papers has led the Bank to strengthen its previous approach to business continuity by assessing the firm's critical services and the supporting processes to identify potential disruptions that could crystallise under various operational scenarios i.e. cyber-attacks or head office unavailability. These detailed assessments have allowed a much greater understanding of where to devote resources to provide effective resilience for these critical services.

The impact of COVID-19 has tested our Operational Resilience Framework during the past two years and has proven appropriate during this time. Feedback from this process has led to refinements and improvements to different aspects of our operational resilience that have strengthened it further. Previous reliance and focus on physical back up sites has been replaced with a more decentralised approach of remote and virtual working practices.

Operational resilience coupled with the financial resilience assessed through the recovery planning outlined above combines to provide a firmwide resilience framework that approaches and tests resilience of the Bank from multiple viewpoints and scenarios.

Report by John Barbour,

Chair of the Audit Committee



The financial period ended 30 September 2021 saw a continuation of COVID-19, with all the disruption and uncertainty that entailed. As a result, as with 2020, all Audit Committees have been held remotely. We look forward in 2021/22 to hold at least some of the meetings on a face-to-face basis. The biggest change within the Group during the course of 2020/21 has been the sale of Hodge Life. With the sale, the Audit Committee decided, with Board approval, that the primary published financials for the Group would be those for Julian Hodge Bank Limited, as this is now the primary operating company within the Hodge Group.

There have also been a number of changes to the composition of the Audit Committee. I would like to offer my deepest thanks to the retiring Alun Bowen for his support during my tenure as Chair of Audit Committee. His humour and historical knowledge of the organisation will be greatly missed. With the sale of Hodge Life, David Gulland has resigned as a Member of the Audit Committee and will be taking up the role of Chairman of Hodge Life under its new owners. The Members of the Audit Committee wish him all the best for the future in his new role. Finally, I accepted Alison Halsey's resignation for personal reasons with regret.

The Audit Committee's agenda continues to include its responsibilities as the third line of defence in Hodge's Risk Management Framework; oversight of the performance and effectiveness of internal and external audit; ensuring the integrity of the financial statements of all companies within the Group; and oversight of Hodge's system of internal control.

Financial and Regulatory Reporting

As mentioned above, with the sale of Hodge Life, the focus of the Audit Committee for financial and regulatory reporting shifts to Hodge Bank. The Committee's main responsibility in relation to the Bank's financial statements is debating and challenging the judgements made by management and questioning the assumptions and estimates on which they are based. The exercise of appropriate judgement in preparing the financial statements is critical to ensure that the Bank's financial statements are fair, balanced and understandable.

The following are the significant judgements, issues and actions taken by the Committee in relation to the annual report and financial statements. Each of these matters was discussed with EY during the year and, where appropriate, addressed as areas of key audit matters in their audit report.

Report by John Barbour (continued)

IFRS 9 Impairment

Area of focus
The IFRS 9 modelling of expected credit losses relies on the formulation of a number of economic scenarios (positive, neutral and negative) and the allocation of probability weightings to each scenario.

Role of the Audit Committee
The Audit Committee reviewed IFRS 9 provision papers throughout the year. The Committee considered the recommendations made by the CFO and challenged the proposed weightings for the positive, neutral and negative scenarios which underpin the IFRS 9 modelling of expected credit losses.

Conclusion/Action taken
The Committee challenged the weightings for the economic scenarios and deemed the scenarios should be adjusted to reflect a more severe negative potential outcome.

Retirement Mortgages and Reversions – Accounting Methodology and Valuation

Area of focus
Following the sale of Hodge Life the expense assumptions in relation to the Bank's Retirement Mortgages and Reversion models needed to be adjusted to reflect that the cost base was no longer apportioned across both companies. Following a new methodology, the Bank revised its expense assumptions for both portfolios during the year.

Actuarial Services
With the sale of Hodge Life, the in-house services of our actuarial experts will no-longer be available to Hodge. In order to ensure appropriate actuarial expertise, Hodge has appointed Milliman as its actuarial advisors.

Role of the Audit Committee
The Committee reviewed a detailed assumptions paper prepared by the CFO with the assistance of Milliman. The Committee challenged the assumptions and the appropriateness of the expenses included in the actuarial models.

Conclusion/Action taken
The Committee approved the change in the expense assumptions in both models following the sale of Hodge Life.

Valuation of Derivatives

Area of focus
Hodge has a substantial amount of derivative financial instruments, relative to its Balance Sheet size. These hedge the risk to changes in interest rates and yield curves. These derivatives are valued at fair value as at the Balance Sheet date.

A proportion of interest rate derivatives are accounted for under IAS 39 hedge accounting rules. Significant changes in rates can affect their effectiveness as a hedge, which might lead to income volatility or a different accounting treatment.

Role of the Audit Committee
The Committee obtained confirmation from management that the valuation of derivatives at the year-end are in accordance with the amounts recognised by the relevant counterparties and that the hedge effectiveness calculations had been carried out appropriately.

Management were also able to evidence, for all the derivatives settled in the year, that the value attributed by counterparties prior to breaking the derivative was in line with the valuation held by the Bank.

Conclusion/Action taken
The Committee was satisfied that the fair value of the derivatives was appropriately reflected in the financial statements and that, where hedge accounting was applied, it was effective.

Long-Term Viability Statement

Area of focus
The directors make a statement in the Annual Report as to the long-term viability of Hodge. The Committee provides advice to the Board on the form and content of the statement, including the underlying assumptions. Once again, the Committee needed to consider the uncertainties associated with COVID-19 as part of its deliberations.

Role of the Audit Committee
The Committee reviews the Board's assessment of long-term viability through consideration of the Bank's rolling five-year strategy, the Bank's assessment of capital (ICAAP) and the Bank's assessment of liquidity (ILAAP). In addition, the Committee specifically considered the impact of potential loan losses due to COVID-19 and the impact on Hodge's capital position.

Conclusion/Action taken
The Committee agreed to recommend the long-term viability statement to the Board.

Fair, Balanced and Understandable Reporting

Area of focus
Hodge endeavours to ensure that its external reporting is fair, balanced and understandable. The Committee undertakes an assessment on behalf of the Board in order to provide the Board with assurance that it can make the statement recommended by the Financial Reporting Council's Corporate Governance Code.

Role of the Audit Committee
The Committee assessed, via discussion with, and challenge of, management (including the Chief Executive and CFO), as to whether disclosures in Hodge's published financial statements were fair, balanced and understandable. An area of particular focus in the year was a review of the new disclosures associated with Climate Change, including the introduction of ESG disclosures.

Conclusion/Action taken
Having evaluated all of the available information and the assurances provided by management, the Committee concluded and were able to recommend to the Board, that Hodge's published report and financial statements were fair, balanced and understandable.

Report by John Barbour (continued)

External Audit

Given the significant transactional activity during the period, the Audit Committee requested a one-year extension to the tenure of Ernst and Young audit partner Andy Blackmore in order to safeguard the quality of the audit. A formal review of the effectiveness and audit quality of EY was carried out in 2021 following closure of the 2020 accounts, including an assessment of the professional scepticism and objectivity of the EY team. The Committee is responsible for assessing the objectivity and independence of EY. This responsibility was discharged through the Audit Committee meetings and during private meetings with EY.

The Committee has a policy whereby all services which are not covered in the audit are approved by the Committee. The Bank continues to examine non-audit fees in light of the Ethical Standard issued by the Financial Reporting Council (FRC). The payments made to EY for non-audit fees in the year ended 30 September was £nil (2020: nil). This reflects a non-audit fee to audit fee ratio of nil%, the average for the last three financial years is nil. The average non-audit fee for the last three financial years is below the 70% limit set by the FRC.

Internal Audit

Deloitte has taken up its role as Internal Auditor and has justified the confidence placed in them upon their selection, demonstrating good engagement with management, executive, Audit Committee and the Board.

The Committee scrutinises and agrees Internal Audit's plans, including agreeing the areas of focus, which this year included IT testing, ILAAP, a credit review, model risk and customer communications.

The Committee tracks the implementation of the recommendations of Internal Audit, in conjunction with Deloitte, and is satisfied that these are being implemented on a timely basis.

A review of the effectiveness of the Internal Audit function was carried out by the Audit Committee. The enhanced presence at committees of Deloitte representatives, especially that of the responsible partner, was a noted benefit. Some small recommendations for improvements were made. The findings were discussed with Deloitte in a private meeting.

Internal Control

The Audit Committee has responsibility on behalf of the Board for Hodge's systems of internal control. The Audit Committee discharges this responsibility by discussing and challenging reports issued by Internal Audit. Further, through my membership of the Risk and Conduct Committee, I am made aware of any issues raised by the second line of defence assurance team which monitors the implementation of its and Internal Audit's recommendations. Collectively these reports provide assurance that there are effective internal controls within the Bank.

The Audit Committee also discusses any control observations raised by EY. The Audit Committee continues to encourage management to reduce the volume of manual internal controls and automate as many controls as possible to reduce operational risk.

Whistleblowing

I am the Whistleblowing Champion for Hodge and have reviewed the integrity, independence and effectiveness of Hodge's whistleblowing policies and procedures and also those policies and procedures intended to protect whistle-blowers from being victimised. The Senior Independent Director has drawn attention to areas for improvement and, as a result, a process is underway to further enhance a culture of "speaking out" within Hodge and new communication and education tools will be rolled out in 2021/22. However, notwithstanding the need for improvement, I am satisfied that current policies are adequate.

Report by John Barbour (continued)

Committee Composition and Meetings

The Committee's membership is designed to provide the depth of financial expertise and commercial acumen it needs to fulfil its responsibilities.

Committee meetings were attended by the Chief Executive, CFO, Head of Risk, Head of Compliance, representatives of Deloitte and EY and by other members of the business, as appropriate.

During the year private meetings were held with the Lead Audit Partner from EY, as well as the Head of Internal Audit from Deloitte, without management present.

Interaction with Regulators

As Chair of the Audit Committee I meet with the members of Hodge's Regulatory team at the PRA, without management present, during their annual visit to Hodge.

Committee Performance

The Committee updated its self-assessment of its performance and concluded that the changes from previous assessments had now been appropriately implemented. One of the issues outstanding was training for members of the Committee. This is now being addressed through individual plans agreed with the Chairman of the Board.

Looking Ahead

In a year of fires, floods and record-breaking temperatures around the world the impacts of climate change become increasingly apparent. The Bank continues to develop its response to climate change. We continue to work on becoming more efficient in the amount of energy we consume as a business, increasing the effectiveness of recycling programmes and improving colleague awareness of environmentally responsible behaviour such as reducing paper, energy and personal car use. Please see the s172 Statement where the Bank has published information to comply with the Streamlined Energy & Carbon Reporting (SECR) initiative for the first time.

John Barbour
Chairman of the Audit Committee
6 December 2021

Report by Iain Laing,

Chair of the Risk and Conduct Committee

> Ongoing frequent dialogue with the regulators remained throughout the pandemic.

Committee Role and Responsibility

Risk and Conduct Committee is a sub-committee of the Board and has delegated authority to assist the Board in fulfilling its oversight responsibilities for risk management.

The Committee is responsible for:

- Promoting an appropriate risk culture and overseeing the development and implementation of the Enterprise Risk Management Framework (ERMF) and associated policies;
- Monitoring our current and emerging risk profile and ensure that these are appropriately mitigated;
- Reviewing and recommending risk appetite to the Board and monitoring our risk profile within this appetite;
- Reviewing and recommending to the Board key prudential documents (ILAAP, ICAAP and the Recovery Plan).

Committee Membership

Iain Laing has been the Chair of the Risk and Conduct Committee throughout the financial year. The Committee comprises six independent non-executive directors with regular attendance from the CEO, CFO, CRO and the Retail Director and supported as required by other colleagues from across the business to assist in discussions. The Committee met nine times through the financial year along with a supplementary risk workshop for scenario development.

The prescribed responsibilities as Chair of the Risk and Conduct Committees are to safeguard the independence of, and oversee the performance of, both the Risk and Compliance functions. As such there are regular meetings with the members of the Risk team who undertake assurance reviews to ensure that the work they are doing, as part of the second line of defence, is as effective as possible and enable them to air any issues and views.

Interaction with management

Both committees are mindful of the need to hold management directly accountable when issues have arisen and been reported by the CRO, Head of Compliance or other parties. Members of senior management attend Committee meetings for deeper discussions in such instances.

The Chair meets with the CRO twice a month to ensure close coordination of efforts and early identification of any issues.

Interaction with regulators

The Committee tracked progress of closure of actions arising from the annual supervisory visit and reviewed management's response to the PRA of confirmation of action completion.

The annual regulatory visit for 2020/21 was postponed due to COVID and will take place in Q4 2021. Ongoing frequent dialogue with the regulators remained throughout the pandemic.

Committee performance

Each committee carried out a self-assessment of its performance as well as a review of its Terms of Reference. The results from the former were satisfactory with the suggested actions implemented. Minor changes to the Terms of Reference have been made.

Report by Iain Laing (continued)

Activities during the year – as highlighted last year

The table below shows the areas highlighted in last year's report on which we planned to focus during this year, and the actions taken.

Area	Progress during 2020/2021
Continued development of credit management capabilities, policies, and controls, including embedding capital considerations into pricing and lending decisions.	A new overarching Credit Risk Framework was developed and put in place with the linked Retail Credit Risk policy and Commercial Credit Risk policy all revised and approved. Deep dives into the Retail and Commercial portfolios through the year explored the capital allocation into the pricing models along with the assumptions being used.
Ensuring the strengthening of retail credit capabilities keeps pace with the growth of retail exposures.	Recruitment for a Head of Credit Risk in the Retail business and a Credit Risk Oversight Manager in the Risk function were completed in the year strengthening both 1st and 2nd lines of defence. The retail deep dive highlighted the advances in credit risk experience these hires have brought.
Ensuring the down-side risks of the commercial credit portfolio are managed proactively.	A full portfolio review took place in commercial in light of COVID developments and Committee has required that this assessment is refreshed quarterly and presented back on any emerging risks or changes in the portfolio.
Continued oversight over the new products and change initiatives required by the Bank's strategy.	Oversight of the Product Committee has been provided to the Committee through regular summaries along with any material product proposals/business proposals put to RCC for challenge and oversight. A new board level committee, the Innovation and Change Committee has been put in place to provide focused challenge and oversight of changes with risks escalated to Risk and Conduct Committee, this is supported by a deep dive on IT change presented to the Committee earlier this year.
Continuing the programme of improvements to the Bank's Risk and Compliance Frameworks.	A revised principal risk hierarchy was approved and new risk management frameworks for each of the principal risks developed, challenged and approved by committee. A new compliance framework was constructed and presented to committee. Climate change has been integrated into the Risk Management Framework, this will continue to develop and mature over the coming years.
Strengthening fraud and financial Crime control.	Fraud specialist resource was recruited into the 1st line business specifically in Retail. Further KYC role is being sought for Commercial lending to bring the skills in-house. The SIRA fraud solution was put live in the business. An overarching financial crime framework has been put in place to bring together all elements of financial crime and fraud in a more cohesive manner.
Ensuring effective first line of defence ownership of all risks.	Committee has supported a significant investment in 1st line resources to improve and take ownership of business line risks. This has been supported by the setting up of new 1st line committees to provide improved governance over risks at an Executive level. The principal risk frameworks put in place support this strengthening by outlining clear roles and responsibilities and guidance on risk management.
Establishing responsibilities for identification and management of financial risks of climate change.	The Responsibilities for climate change have been allocated and a plan in place to ensure development of management of financial risk for climate change which is on track for compliance by the end of the calendar year. A risk identification exercise was undertaken with stakeholder engagement from across the business to draw out all our potential exposures. The Board's ambition for climate change has been set.

Report by Iain Laing (continued)

Significant risks and areas of focus

In addition to the activities signposted from last year discussed above, the significant matters addressed by the Committee during the year are summarised in the following table.

Area	Risk and Conduct Committee Activity
Enterprise Risk Management	Requesting and overseeing the development of a new suite of principal risk management frameworks. Approved changes to the risk appetite to align to the frameworks and challenged management to develop a more concise and targeted set of risk appetites. Committee receive regular summaries of risk profile through the Chief Risk Officer's report. The Committee reviewed and approved a 1st line compliance gap analysis and action plan following the improvements put in place to develop 1st line risk ownership.
Frameworks and policies	The Committee approved proposed improvements to the Risk Management Framework through the implementation of new principal risk hierarchy. The Committee approved a revised compliance framework. The Committee approved several financial risk policy updates.
Risk Management	The Committee requested a review of the nature of the information provided to ensure greater focus on the key drivers of risk. The Committee approved the risk assurance and compliance monitoring plans for the year. The Committee oversees quarterly summaries on the 2nd line assurance reviews
Risk Monitoring	Committee defines the agenda for a programme of risk deep dives into areas of focus, this year covered; • Retail credit risk • Commercial credit risk • 3rd party risk management • Complaints • IT Change • 3rd party assurance provided on cyber security controls and progress of action closure against previous year. The Committee receives regular reports on the enterprise-wide risk profile of the business. Incidents were raised throughout the period, those of material nature were supported by remediation plans and lessons learnt assessments. Committee were satisfied with the actions being taken.
Financial resilience and stress testing	During the year the Committee, supported by the Risk Function: • Reviewed and challenged the design and execution of the capital and liquidity adequacy assessment processes (ICAAP and ILAAP), including any changes to methodology and assumptions. • Reviewed and challenged the Recovery Plan document. • Approval and recommendation to Board for the ICAAP, ILAAP and Recovery Plan. • The Committee supported the move of the Recovery Plan document ownership moved from 2nd line back into 1st line. • The Committee monitors progress on transition from LIBOR.
COVID	• The Committee oversees the top and merging risks with COVID a material feature that is a constant in discussions. • Conduct deep dives for credit portfolios in place to identify any deterioration in credit quality. • Cyber security deep dive exploring the different threat profile from a working from home environment.

Report by Iain Laing (continued)

Area	Risk and Conduct Committee Activity
HLAC sale and transition risks	As noted, a material subsidiary of the Group disposal took place this year and committee reviewed updates on progress and risks posed to the Bank by this transition to disposal.
Climate	The Committee oversees progress with the climate risk implementation plan to ensure compliance in 2021. Committee approved the recommended approach to climate risk financial risk assessment modelling. Committee discussed the incorporation of climate change risk into the Risk Management Framework.

Looking ahead

Iain Laing, Chair of the Hodge Bank Risk and Conduct Committee, will be encouraging the Committee to focus on the following areas during the next financial year:

- Ensuring the strengthening of retail credit capabilities keeps pace with the growth of retail exposures;
- Continue to monitor the external environment and the potential COVID implications particularly as government support is unwound;
- Ensuring effective management of the risks posed by third parties and outsource providers;
- Continued oversight over the new products and change initiatives required by the strategy;
- Continuing the programme of improvements and maturity for the Bank's risk and compliance frameworks;
- Embedding and maturing the management of financial risks of climate change;
- Continuing development of the management information to support risk management across the business.

Iain Laing
Chair of Risk and Conduct Committee
6 December 2021

Report by Graeme Hughes,

Chair of the Nominations and Governance Committee

> We have engaged in a number of valuable and key appointments to Hodge.

As Chair of the Nomination Committee, we have engaged in a number of valuable and key appointments to Hodge over the last 12 months. Rebecca Hall was appointed by the Group in a non-executive role to support the sale of our HLAC business, with Rebecca Hall joining HLAC in October 2020. At executive level, David Landen was appointed to the CEO role on a permanent basis in September 2020. David first joined Hodge as a graduate in 2002, so this was a wonderful example of growing talent and succession planning in practice. His appointment also led to the vacancy of a Chief Finance Officer. Initially, we filled this on an interim basis with Richard Jones, whilst we looked to source and appoint a permanent CFO. I am delighted to say that Jan Preece joined us from Aviva in September 2021. A further Executive Board appointment was made with Matt Burton becoming Retail Director, taking responsibility for our Retail, Savings and Operations teams and building new capability in the area of customer experience and continuous improvement. This was another great internal appointment for Hodge. The search for a new Senior Independent Director is underway following the resignation of Alison Halsey.

The Nomination Committee also reviewed the strength and depth of our board and executive succession planning. It was noted that our talent and succession had strengthened from the previous period, with many examples of internal career progression and promotions as highlighted above. Where succession gaps existed, focused recruitment activity was underway to strengthen the talent pipeline in these teams. For our Non-Executive and Board members, we introduced a new performance review and development approach, that set focused objectives and development planning with these conversations led by me as Chair. A Board development plan was rolled out which included sessions on `COVID and the Customer', 'Capital Markets and M&A', 'Technology and Change' and deep dives on all aspects of our business.

Finally, the Nomination Committee wanted to provide additional scrutiny of and adopt delegated Board responsibility for ED&I at Hodge given the strategic importance of a fully inclusive culture. At Hodge, we knew we had work to do. We needed to do more to raise colleague awareness of the benefits of providing diversity profile data, to adopt recruitment practices that encouraged applications from diverse groups and also to encourage our colleagues to engage in the plans to make Hodge a more diverse and inclusive place to work and thrive. Over the last 12 months, the Nomination Committee approved a new ED&I strategy that sets out our ambition and commitments. It is supported by a newly created ED&I Network promoting allyship and Hodge has also signed up to the Race at Work charter with Business in the Community as well as committed to be a Disability Confident Leader. We are now into our second year of the Women in Finance Charter too.

Report by Graeme Hughes (continued)

In the spirit, of keeping honest and also assessing ourselves against best in class, Hodge joined the Financial Services Culture Board and conducted its first survey in September 2020. A second survey followed in June 2021. Early reporting has shown us improve by an average of four points in 29 out of 36 questions. Areas of focus for us going forward, remain engaging our colleagues further in our shared purpose and continuing to improve on our customer experience and services.

Next year will see the Nomination Committee held to account for the plans that support the ED&I strategy, ensuring good progress is being made on our pledges and commitments. Our purpose, values and behaviours are about to be shared through an engaging series of colleague events and activities, as we look to bring to life our employee value proposition to new and existing colleagues. As we enter into a new performance year shortly, we will build on our board expertise through focused development sessions that offer ongoing stretch and challenge on those topics that build resilience and future success.

As I conclude this report, I want to thank Helen Molyneux who has been a non-executive member of the Nominations Committee and Chair of the Remuneration Committee for her excellent service to Hodge and the Board. Helen leaves Hodge in December 2021 and as the longest serving NED, having completed 6 years on the Board. Her expertise, judgement and support has been invaluable throughout this time.

Graeme Hughes
Chair of the Nominations and Governance Committee
6 December 2021

Report by Helen Molyneux,

Chair of the Remuneration Committee

> This year a higher than usual number of senior appointments were made.

The 2020/21 financial year proved to be an extremely busy time for the Remuneration Committee. The Committee met, remotely via video conference, on nine separate occasions dealing with a full agenda of remuneration issues throughout the year.

Having established a remuneration strategy last year, the Committee requested and approved the development of a remuneration policy to support its decision making. The draft policy was reviewed by Deloitte prior to approval, who provided invaluable feedback, ensuring that our policy is CRDV compliant and that the identification and consideration of material risk takers in the remuneration sphere has been properly considered. This policy has stood us in good stead as we have navigated the Remuneration Committee's agenda throughout the period.

This year a higher than usual number of senior appointments were made which required benchmarking exercises to be conducted by the Committee. Salary and benefit packages were considered and agreed for the new CEO, Retail Director, Interim CFO and CFO, taking into account the Bank's financial position, its strategy for the future and its growth plans. The annual pay review was also considered by the Committee against the backdrop of the pandemic, its impact on business and our employees. Our view was that, despite the financial impact of the pandemic, our colleagues had taken on the additional pressures created with commitment and fortitude and should therefore be rewarded for their efforts with a small pay increase pending a more widespread job levelling and benchmarking exercise being conducted. Having benefitted from the Furlough scheme in 2020, no further payments were sought under that scheme after September 2020.

The job levelling and benchmarking exercise was carried out with the support of Towers Watson and reported to the Committee in April, to provide reassurance as to the appropriateness of remuneration within the business. This was the first time that a comprehensive review had been conducted of the salary bands and grades within the organisation, applying various lenses, including that of gender, to ensure that we are both competitive in the market place and fair to our existing colleagues. As a consequence, a number of salary increases were approved to ensure parity of approach across all colleagues.

We had postponed our review of gender pay last year as a result of the pandemic but completed it this year for publication and reporting. The report shows that we have some

Report by Helen Molyneux (continued)

work to do to ensure that our female colleagues are fully represented at all levels (particularly the more senior levels) within the organisation, but where colleagues are doing the same jobs, they are paid equally. We will be focussing this coming year on how we ensure that promotion opportunities and senior roles are more evenly balanced by gender and ethnicity.

In addition to the salary benchmarking exercise, a review of core benefits was also undertaken with a view to ensuring that the benefits traditionally provided by Hodge were still appropriate and valuable. As a result, some changes were made to the benefits offered to all employees to ensure that they are both fit for purpose and competitive in the marketplace – including an increase in holiday entitlement for most of our colleagues.

We also conducted a review of our pension scheme. Hodge has traditionally considered its pension benefit to be a key plank of its remuneration strategy and has provided all colleagues with a defined benefit scheme. Over the last few years, however, it became apparent that the cost of such a scheme meant that we were unable to offer a range of other benefits to our colleagues, depending on their stage in life and what was important to them at the time. Following a detailed consideration of the alternatives and a full consultation process with our colleagues and the Shareholder, a new defined contribution scheme was introduced in April and all colleagues have been transitioned to the new scheme.

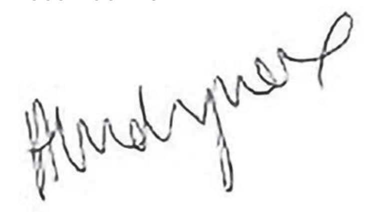
The final piece of the remuneration jigsaw – performance related pay – was also on the agenda this year. The Committee approved the Annual Reward Plan for all colleagues, which is designed to pay a bonus to all colleagues provided that a balanced scorecard of measures is met, focussing on delivering the best service to our customers, product innovation, conduct, financial performance and the sustainability of the business. On reviewing the result of the scheme, the Committee exercised its discretion to revise the gateway conditions for payment under the scheme as, as a result of the sale of HLAC, the financial metrics were not met. As the failure to meet the financial targets was a direct result of strategic decisions made by the Board it was decided that our colleagues should not be penalised, especially bearing in mind the considerable effort and achievement involved in achieving the strategic objectives. The Committee therefore agreed an amendment to the balanced scorecard calculations which enabled an appropriate bonus payment to be made to all colleagues.

For our senior leadership team, we considered the implementation of a long term reward plan starting in September 2021, again focussed on a balanced scorecard of measures which we believed would deliver against our strategic objectives and, importantly, align our leaders with the key objective of increasing shareholder value over the next 4 years. After consultation with the Shareholder, a decision was taken to postpone implementation and review the plan against the revised strategy and 5 year forecast in January 2022. The revised scheme will aim to provide an appropriate level of incentive to the executive team within a meaningful timescale whilst, taking into account Provision 40 of the UK Corporate Governance Code focussing on delivering a sustainable, long term, profitable organisation for the benefit of our shareholders, colleagues and customers.

The Shareholder has been consulted on a regular basis on the key strategic matters before the Remuneration Committee, including the design of the annual reward scheme and the executive reward scheme, to ensure that the schemes align with shareholder interests.

This is my final report as Chair of the Remuneration Committee as I will be standing down in December. The last year has been a challenge for many of our colleagues, working remotely and with the added pressures that the pandemic has placed upon us all. I would therefore like to express my particular thanks and gratitude to the members of the Committee and to the supporting executives, including the Chief People Officer, for their hard work, diligence and wise contributions to the very wide range of matters that we had to deal with throughout my time as Chair and I wish you well for the future.

Helen Molyneux
Chair of the Remuneration Committee
6 December 2021



Report by Aileen Wallace,

Chair of Innovation and Change Committee

> I was delighted to implement the Board Innovation and Change Committee.

On joining the Board in early 2020, I was delighted to implement the Board Innovation & Change Committee and become Chair. As the Bank is recognised as a firm that actively embraces technology in support of its purpose of making life better for customers and society in moments that matter, the Committee's creation was a key part of ensuring the appropriate level of assurance was afforded to this important strategic goal.

In its first year, the Committee has met quarterly, with a dedicated terms of reference and standard operating agenda ensuring proportionate focus on strategic key drivers such as technical resilience, frictionless change execution, IT talent enablement and overall organisational digital capability. Membership of the Committee during the year included our two executive directors and a compliment of non-executive members from both Hodge Bank and Hodge Life Assurance, assisting the Board in fulfilling its wider corporate governance and oversight responsibilities in relation to the Bank's execution of technology programmes and investments initiated in support of the our strategy. Close working relationships have been forged between the Committee and the Bank's Risk & Conduct Committee in the last year on key risk areas such as cyber, information systems strategy and data, ensuring appropriate focus on key risk mitigation factors underpinned by technical solutions.

Interaction with management

The Committee has been conscious of the need to also engage informally with management and in support of our objective, as Chair, I have held monthly meetings with the Chief Technology Officer and the Group Retail Director/Deputy CEO. These meetings have been valuable in ensuring there is common appreciation and understanding of industry themes, particularly in digital enablement and the evolving cyber landscape, and in the dynamic review of our information systems strategy, which the Committee were pleased to note was assessed favourably as part of an external assurance review.

Future ways of working

As we move into a newly framed external working environment driven by the response to COVID, there has never been a greater demand for digital transformation. A global workforce now exists enabling individuals with critical skills, operating independently from home, to work flexibly. However, the enormous change brought about by the uncertainty and impact of COVID has placed an even greater focus on values driven impact, such as organisational and employee purpose. During the last year, the Committee carefully provided oversight of our employee value proposition and specifically how this relates to technical and digital role holders, making a number of enhancements including providing time and support to learn and undertake innovation sprints. The Committee gained assurance with management's review of the technical and leadership skillsets in place to continue to fulfil our strategic objectives, including wider engagement with colleagues on future workplace location strategies and the strength of our digital leaders

Report by Aileen Wallace (continued)

succession planning. The Committee additionally reviewed plans to efficiently utilise the skills of key partners in the execution of our digital savings platform programme, and were pleased to see the depth in both the selection process and strong partner brand alignment, thereby enabling the Committee to recommend support of these to the Board.

Committee performance and composition

The Committee carried out a self-assessment of its performance including a review of its terms of reference. Minor changes to the terms of reference have been made as a result. In light of the sale of Hodge Life Assurance, the Committee, with its focus solely on Hodge Bank has seen a new member join, namely Graeme Hughes, Chair of the Hodge Bank Board. We wish David Gulland, our Hodge Life Assurance non-executive member well and thank him for his support and contributions to the Committee during the last twelve months.

Looking ahead

Having spent its inaugural twelve months ensuring the Bank is well positioned to take advantage of digital opportunities and key partnerships to deliver on it's purpose to make life better for customers and society, the Committee has clearly laid the necessary foundations and built a future centric governance infrastructure. Simplification and efficiency are core tenets of innovation and with this in mind, over the year ahead, the Committee will be focusing on;

- Supporting our executive team in elevating their innovative thinking in delivering unique value-added benefits and ensuring core building blocks are delivered.
- Monitoring our talent programmes and industry responses to continuing digital demand.
- Ensuring optimal outcomes from our new 3rd party delivery partnership, where we can leverage scale and optimise resources.
- Ongoing development of our cost benefit analysis to ensure that we remain on track to deliver our planned technology strategy.
- Innovating our responses to the cyber threat landscape, meeting pace with pace.

Aileen Wallace
Chair of the Innovation and Change Committee

6 December 2021

Directors' Report

The directors present their report together with the audited financial statements for the year ended 30 September 2021. Certain disclosures are given in the Chairman's Statement, Strategic Report and the financial statements and are incorporated here by cross-reference. Specifically, these incorporate the following disclosures:

Group strategy - page 8

Financial performance review - page 18

Risk management policies - page 30

Derivative financial instruments - note 22

Directors and directors' interests
The directors who held office during the year were as follows:

David Landen (CEO)

Matthew Burton (Deputy CEO)

Jan Preece (CFO)
(Appointed September 2021)

Richard Jones (Interim CFO)
(Resigned September 2021)

Graeme Hughes* (Chairman)

Alun Bowen* (Non-Executive Director)
(Resigned December 2020)

Aileen Wallace* (Non-Executive Director)

Iain Laing* (Non-Executive Director)

Helen Molyneux* (Non-Executive Director)

John Barbour* (Non-Executive Director)

Alison Halsey* (Non-Executive Director)
(Resigned August 2021)

No contract was entered into by the Bank in which a director had a material interest.

* All non-executive directors are deemed to be independent by the Board. None of the directors held any interests in the shares of any group companies.

During the year, there were no contracts entered into by the Bank in which the directors had a material interest.

Political contributions
The Bank made no political contributions during either year.

Post Balance Sheet events
There were no post Balance Sheet events to disclose.

Dividend
No dividends have been declared or paid during the year.

Qualifying third-party indemnity provisions
The Bank has granted an indemnity to one or more of its directors against liability in respect of proceedings brought by third parties, subject to the conditions set out in the Companies' Act 2006. Such qualifying party indemnity provisions remain in force as at the date of approving the Director's Report.

Re-appointment of auditors
A resolution for the re-appointment of EY as auditor of the Company is to be proposed at the forthcoming Annual General Meeting of the Company's parent, The Carlyle Trust Limited.

Going concern
The directors have considered the appropriateness of the going concern basis of preparation of the financial statements taking into account the Bank's current and projected performance, including consideration of projections incorporating the impact of the COVID-19 pandemic on the Bank's capital and funding position. As part of this assessment the Board considered:

- The impact on the Bank's profits from an expected reduction in income from residential and commercial lending combined with increased credit impairment charges;
- The sufficiency of the Bank's capital base, which is expected to be sufficient to weather even a severe COVID-19 related downturn; and,
- The adequacy of the Bank's liquidity.

The Bank's forecasts and projections include scenario testing undertaken in accordance with the Internal Capital Adequacy Assessment Process and Internal Liquidity Adequacy Assessment Process, which are required by the Prudential Regulation Authority to demonstrate appropriate levels of capital and liquidity respectively under stressed conditions.

The directors confirm that they are satisfied that the Bank will continue in business for a period of fifteen months to 31 December 2022. Consequently, the going concern basis continues to be appropriate in preparing the financial statements.

By order of the Board

David Landen
Director
6 December 2021

Statement of Directors' Responsibilities

Directors' Responsibilities Statement
The directors are responsible for preparing the Strategic Report, the Directors' Report and the financial statements in accordance with applicable law and regulations.

Company law requires the directors to prepare financial statements for each financial year. Under that law they have elected to prepare the financial statements in accordance with UK Accounting Standards and applicable law (UK Generally Accepted Accounting Practice) including Financial Reporting Standard 101 Reduced Disclosure Framework (FRS 101).

Under company law the directors must not approve the financial statements unless they are satisfied that they give a true and fair view of the state of affairs of the Company and of the profit or loss of the Company for that period. In preparing these financial statements, the directors are required to:

- select suitable accounting policies and then apply them consistently;
- make judgements and estimates that are reasonable and prudent;
- state whether applicable UK Accounting Standards have been followed, subject to any material departures disclosed and explained in the financial statements; and
- prepare the financial statements on the going concern basis unless it is inappropriate to presume that the Company will continue in business.

The directors are responsible for keeping adequate accounting records that are sufficient to show and explain the Company's transactions and disclose with reasonable accuracy at any time the financial position of the Company and enable them to ensure that the financial statements comply with the Companies Act 2006. They have general responsibility for taking such steps as are reasonably open to them to safeguard the assets of the Company and to prevent and detect fraud and other irregularities.

The directors are responsible for the maintenance and integrity of the corporate and financial information included on the Company's website. Legislation in the UK governing the preparation and dissemination of financial statements may differ from legislation in other jurisdictions.

Each of the directors who is a director at the date of the approval of this Annual Report confirms to the best of their knowledge:

- The Bank's financial statements prepared in accordance with FRS 101, give a true and fair view of the assets, liabilities, financial position and profit or loss of the Bank.
- The Strategic Report includes a fair view of the development and performance of the business and the position of the Bank together with the description of the principal risks and uncertainties that it faces.
- The Annual Report, taken as a whole, is fair, balanced and understandable and provides the information necessary for the shareholder to assess the Bank's position and performance, business model and strategy.
- The directors who held office at the date of approval of this Directors' Report confirm that, so far as they are each aware, there is no relevant audit information of which the Bank's auditor is unaware; and each director has taken all the steps that he ought to have taken as a director to make himself aware of any relevant audit information and to establish that the Bank's auditor is aware of that information.

By order of the Board

David Landen
Director
6 December 2021

Auditor's Report

Independent Auditor's Report to the Member of Julian Hodge Bank Limited

Opinion

We have audited the financial statements of Julian Hodge Bank Limited for the year ended 30 September 2021 which comprise the Income Statement, Statement of Other Comprehensive Income, Balance Sheet, Statement of Changes in Equity and the related notes 1 to 30 (except for the sections of note 29 which are marked as unaudited), including a summary of significant accounting policies. The financial reporting framework that has been applied in their preparation is applicable law and United Kingdom Accounting Standards including FRS 101 "Reduced Disclosure Framework" (United Kingdom Generally Accepted Accounting Practice).

In our opinion, the financial statements:

- give a true and fair view of the Company's affairs as at 30 September 2021 and of its profit for the year then ended;
- have been properly prepared in accordance with United Kingdom Generally Accepted Accounting Practice; and
- have been prepared in accordance with the requirements of the Companies Act 2006.

Basis for opinion

We conducted our audit in accordance with International Standards on Auditing (UK) (ISAs (UK)) and applicable law. Our responsibilities under those standards are further described in the Auditor's responsibilities for the audit of the financial statements section of our report. We are independent of the Company in accordance with the ethical requirements that are relevant to our audit of the financial statements in the UK, including the FRC's Ethical Standard as applied to public interest entities, and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Conclusions relating to going concern

In auditing the financial statements, we have concluded that the directors' use of the going concern basis of accounting in the preparation of the financial statements is appropriate. Our evaluation of the directors' assessment of the company's ability to continue to adopt the going concern basis of accounting included:

- In conjunction with our walkthrough of the Company's financial close process, we confirmed our understanding of management's going concern assessment process, and confirmed their assessment covered all key factors;
- We evaluated management's going concern assessment, which included reviewing their evaluation of long-term business and strategic plans, capital adequacy, liquidity, and funding positions. We also verified that the Company's risk management practices were considered, including credit risk, market risk and operational risks;
- We have agreed key data in management's going concern assessment to underlying workings and other supporting documentation;
- We assessed the results of management's stress testing, including consideration of principal and emerging risks relating to funding, capital, and liquidity;
- We reviewed the future profit forecasts, including assessing the reasonableness of assumptions, and historical forecasting accuracy;
- We reviewed correspondence with the regulators for any matters that may impact going concern assessment; and
- We evaluated the adequacy of the directors' disclosure in relation to going concern in the Directors' Report and notes to the financial statements.

Based on the work we have performed, we have not identified any material uncertainties relating to events or conditions that, individually or collectively, may cast significant doubt on the Company's ability to continue as a going concern for a period of fifteen months to 31 December 2022.

Our responsibilities and the responsibilities of the directors with respect to going concern are described in the relevant sections of this report. However, because not all future events or conditions can be predicted, this statement is not a guarantee as to the Company's ability to continue as a going concern.

Overview of our audit approach

Key audit matters	• The risk that inappropriate actuarial assumptions are used in the valuation of investment properties (reversionary interest in properties). • The risk that inappropriate property / collateral valuations are applied in the calculation of the IFRS 9 expected credit loss ('ECL') provision (Stage 3 credit impairment provision on loans and advances to customers). • The risk of incorrect valuation of derivatives.
Materiality	• Overall materiality of £2.2m which represents 1.5% of equity.

An overview of the scope of our audit

Tailoring the scope
Our assessment of audit risk, our evaluation of materiality and our allocation of performance materiality determine our audit scope for the Company. This enables us to form an opinion on the financial statements. We take into account size, risk profile, the organisation of the Company and effectiveness of controls, including controls and changes in the business environment when assessing the level of work to be performed. All audit work was performed directly by the audit engagement team.

Key audit matters
Key audit matters are those matters that, in our professional judgment, were of most significance in our audit of the financial statements of the current period and include the most significant assessed risks of material misstatement (whether or not due to fraud) that we identified. These matters included those which had the greatest effect on: the overall audit strategy, the allocation of resources in the audit; and directing the efforts of the engagement team. These matters were addressed in the context of our audit of the financial statements as a whole, and in our opinion thereon, and we do not provide a separate opinion on these matters.

Risk	Our response to the risk	Key observations communicated to the Audit Committee
The risk that inappropriate actuarial assumptions are used in the valuation of investment properties (reversionary interest in properties: £94.6m, 2020: £97.4m). Refer to the accounting policy for - Investment properties – reversionary interests in properties and Note 17 to the financial statement. The valuation of investment properties is highly judgemental as it relies upon a number of assumptions with high estimation uncertainty, including those in respect of the discount rate, policyholder mortality/longevity, expenses, and property price underperformance. Management engaged an external actuarial specialist to determine the actuarial assumptions to be used in the valuation of investment properties. Inappropriate assumptions may lead to a material misstatement in the financial statements.	We performed a walkthrough to understand the assumption setting process including design of controls. We took a substantive approach in evaluating appropriateness of actuarial assumptions used in the valuation of investment properties. We evaluated the competence, capabilities and objectivity of management's actuarial specialist. We engaged internal actuarial specialists to assist the audit team in auditing the actuarial assumptions used in the valuation of investment properties. We evaluated the competence, capabilities and objectivity of our internal actuarial specialist. Our internal actuarial specialists considered the appropriateness of each assumption by considering the assumptions applied by others in the sector and the portfolio's own historic experience.	We considered that management's specialist and our internal specialists are objective, competent and capable of assessing the reasonableness of the actuarial assumptions used in the valuation of investment properties. We concluded that the assumptions that are used in the valuation of the investment properties are within a reasonable range, with the majority of assumptions towards the middle of the range.
The risk that inappropriate property/collateral valuations are applied in the calculation of the IFRS 9 ECL provision (Stage 3 credit impairment provision on loans and advances to customers: £5.1m, 2020: £4.8m). Refer to the accounting policy for – measurement of ECL and Notes 14 and 28 to the financial statements The assessment of the expected credit loss provision is inherently judgemental. Given the highly collateralized nature of the loan portfolio, collateral values are the most sensitive variable to the overall ECL calculation.	We performed a walkthrough to understand the IFRS 9 ECL process and tested the controls for the valuation of collateral. We also reviewed the provisioning methodology to verify compliance with IFRS. For a sample of Stage 3 loans we utilised our property valuation specialists to perform an independent valuation of the collateral used within the ECL provision calculation. The sample we tested in our audit covered £16.4m, 99% (2020: £9.2m, 73%) of the collateral value for the Stage 3 loans.	The controls within the process were tested and were found to be operating effectively. The valuation of stage 3 property loans collateral was determined to be within an acceptable range.
The risk of incorrect valuation of derivatives: £14.7m (2020: £82.0m). Refer to the accounting policy for financial instruments – financial liabilities and Note 22 to the financial statements. The Company holds a significant number of derivative financial instruments, which it uses to manage interest rate risk. The valuation of these derivatives is determined through the application of valuation techniques which often involve the exercise of judgement and the use of assumptions and estimates. Due to the significance of the financial instruments and the related estimation uncertainty this is considered a key audit matter.	We performed a walkthrough to understand the derivatives valuation process including design of the controls. We took a substantive approach for the testing of derivative valuation. Utilising our derivative valuation specialists, we independently valued a sample of derivative financial instruments. We compared our independent valuation to management's valuation and considered whether management's value was within an acceptable range. The sample selected covered £15.9m of £19.3m in absolute terms (2020: £74.5m of £84.0m in absolute terms) of the total population.	The valuation of derivatives was determined to be within an acceptable range.

In the prior year, our Auditor's Report included a key audit matter in relation to the risk of incomplete identification of loan assets held at amortised cost with significant increases in credit risk (Stage 2) or credit impairment (Stage 3) on a timely basis, including due to incorrect application of the internal risk and S&P scorecard ratings applied in the commercial loan book. In current year, we no longer deem this to be a key audit matter because based on sensitivity analysis performed, the likelihood and potential magnitude of potential misstatement at year end are such that we do not consider this to represent a significant risk.

In addition to this, our Auditor's Report also included a key audit matter in relation to the use of inappropriate actuarial assumptions in the valuation of equity release mortgages, which is not applicable in the current year due to the sale of that portfolio in the current year.

Our application of materiality

We apply the concept of materiality in planning and performing the audit, in evaluating the effect of identified misstatements on the audit and in forming our audit opinion.

Materiality

The magnitude of an omission or misstatement that, individually or in the aggregate, could reasonably be expected to influence the economic decisions of the users of the financial statements. Materiality provides a basis for determining the nature and extent of our audit procedures.

We determined materiality for the Company to be £2.2 million (2020: £2.4 million), which is 1.5% (2020: 1.7%) of equity. We believe that equity provides us the key stakeholders (including the principal shareholder and the PRA) are focused on the financial strength and solvency position of the business, which is represented in the financial statements by equity.

During the course of our audit, we reassessed initial materiality and confirmed that the final materiality was in line with initial materiality.

Performance materiality

The application of materiality at the individual account or balance level. It is set at an amount to reduce to an appropriately low level the probability that the aggregate of uncorrected and undetected misstatements exceeds materiality.

On the basis of our risk assessments, together with our assessment of the Company's overall control environment, our judgement was that performance materiality was 75% (2020: 75%) of our planning materiality, namely £1.7m (2020: £1.8m). We have set performance materiality at this percentage because our prior year audit experience indicates a lower risk of misstatements, both corrected and uncorrected.

Reporting threshold

An amount below which identified misstatements are considered as being clearly trivial.

We agreed with the Audit Committee that we would report to them all uncorrected audit differences in excess of £0.1m (2020: £0.1m), as well as differences below that threshold that, in our view, warranted reporting on qualitative grounds.

We evaluate any uncorrected misstatements against both the quantitative measures of materiality discussed above and in light of other relevant qualitative considerations in forming our opinion.

Other information

The other information comprises the information included in the annual report, other than the financial statements and our Auditor's Report thereon. The directors are responsible for the other information contained within the annual report.

Our opinion on the financial statements does not cover the other information and, except to the extent otherwise explicitly stated in this report, we do not express any form of assurance conclusion thereon.

Our responsibility is to read the other information and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the course of the audit or otherwise appears to be materially misstated. If we identify such material inconsistencies or apparent material misstatements, we are required to determine whether this gives rise to a material misstatement in the financial statements themselves. If, based on the work we have performed, we conclude that there is a material misstatement of the other information, we are required to report that fact.

We have nothing to report in this regard.

Opinions on other matters prescribed by the Companies Act 2006

In our opinion, based on the work undertaken in the course of the audit:

- the information given in the Strategic Report and the Directors' Report for the financial year for which the financial statements are prepared is consistent with the financial statements; and
- the Strategic Report and Directors' Report have been prepared in accordance with applicable legal requirements;

Matters on which we are required to report by exception

In the light of the knowledge and understanding of the company and its environment obtained in the course of the audit, we have not identified material misstatements in the strategic report or directors' report.

We have nothing to report in respect of the following matters in relation to which the Companies Act 2006 requires us to report to you if, in our opinion:

- adequate accounting records have not been kept, or returns adequate for our audit have not been received from branches not visited by us; or
- the financial statements to be audited are not in agreement with the accounting records and returns; or
- certain disclosures of directors' remuneration specified by law are not made; or
- we have not received all the information and explanations we require for our audit.

Responsibilities of directors

As explained more fully in the Statement of Directors' Responsibilities set out on page 57, the directors are responsible for the preparation of the financial statements and for being satisfied that they give a true and fair view and for such internal control as the directors determine is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, the directors are responsible for assessing the Company's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless the directors either intend to liquidate the company or to cease operations, or have no realistic alternative but to do so.

Auditor's responsibilities for the audit of the financial statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an Auditor's Report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with ISAs (UK) will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these financial statements.

Explanation as to what extent the audit was considered capable of detecting irregularities, including fraud

Irregularities, including fraud, are instances of non-compliance with laws and regulations. We design procedures in line with our responsibilities, outlined above, to detect irregularities, including fraud. The risk of not detecting a material misstatement due to fraud is higher than the risk of not detecting one resulting from error, as fraud may involve deliberate concealment by, for example, forgery or intentional misrepresentations, or through collusion. The extent to which our procedures are capable of detecting irregularities, including fraud is detailed below.

However, the primary responsibility for the prevention and detection of fraud rests with both those charged with governance of the company and management.

- We obtained an understanding of the legal and regulatory frameworks that are applicable to the Company and determined that the most significant are those that related to the reporting framework (FRS 101 and the Companies Act 2006), license conditions and supervisory requirements under the Financial Conduct Authority (FCA) and Prudential Regulation Authority (PRA), the relevant direct and indirect tax compliance regulation in the United Kingdom.
- We understood how the Company is complying with those frameworks by making inquiries of management, those charged with governance and those responsible for legal and compliance matters. We corroborated our inquiries through review of meeting minutes of the Board and the Board committees and internal audit reports and noted that there was no contradictory evidence.
- We assessed the susceptibility of the Company's financial statements to material misstatement, including how fraud might occur by considering the controls that the Company has established to address risks identified by the entity, or that otherwise seek to prevent, deter or detect fraud. We identified the risk of material fraud through management override of controls by assessing revenue, specifically topside manual adjustments to revenue, to be subject to fraud risk. Our audit procedures included testing a sample of journals to verify the transactions were appropriate and supported by source documentation.
- Based on this understanding, we designed our audit procedures to identify non-compliance with such laws and regulations. Our procedures involved making inquiry about the policies that have been established to prevent non-compliance with laws and regulations, inquiring about the company's methods of enforcing and monitoring the compliance with such policies, reviewing complaints log, and inspecting significant correspondence with the FCA and PRA.
- The Company operates in the banking and capital markets industry which is a specialised area. As such, the Senior Statutory Auditor considered the experience and competence of the engagement team to ensure that the team had appropriate competence and capabilities, which included the use of specialists where appropriate.

A further description of our responsibilities for the audit of the financial statements is located on the Financial Reporting Council's website at:

https://www.frc.org.uk/auditorsresponsibilities.

This description forms part of our Auditor's Report.

Other matters we are required to address

- We were appointed by the Company on 22 April 2016 to audit the financial statements for the year ending 31 October 2016 and subsequent financial periods.
- The period of total uninterrupted engagement including previous renewals and reappointments is 6 years, covering the years ending 31 October 2016 to 30 September 2021.
- The non-audit services prohibited by the FRC's Ethical Standard were not provided to the Company and we remain independent of the Company in conducting the audit.
- The audit opinion is consistent with the additional report to the Audit Committee.

Use of our report

This report is made solely to the Company's members, as a body, in accordance with Chapter 3 of Part 16 of the Companies Act 2006. Our audit work has been undertaken so that we might state to the Company's members those matters we are required to state to them in an Auditor's Report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the company and the company's members as a body, for our audit work, for this report, or for the opinions we have formed.

Andy Blackmore
(Senior statutory auditor)
for and on behalf of
Ernst & Young LLP,
Statutory Auditor
Bristol
7 December 2021

Ernst & Young LLP

Financial Statements

Income Statement

For the year ended 30 September 2021

	Notes	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Interest receivable and similar income	4	39.6	38.4
Interest payable and similar charges	5	(22.0)	(22.8)
Net interest income		**17.6**	**15.6**
Fees and commissions receivable		2.5	1.8
Fees and commissions payable		-	-
Net fee and commission income		**2.5**	**1.8**
Investment income		6.0	3.5
Other operating income		0.1	-
Net operating income		**26.2**	**20.9**
Administrative expenses	6	(25.9)	(22.3)
Depreciation and amortisation		(2.4)	(1.8)
Impairment losses on loans and advances to customers	14	-	(5.4)
Operating loss		**(2.1)**	**(8.6)**
Gains arising from the derecognition of financial assets managed at amortised cost	10/11	-	4.2
Other fair value gains / (losses)	7	11.3	(16.7)
Loss on disposal of loans and advances to customers held at fair value	13	(5.5)	-
Profit / (loss) before taxation	**8**	**3.7**	**(21.1)**
Tax credit on profit	9	2.1	5.2
Profit / (loss) for the financial period		**5.8**	**(15.9)**

Statement of Other Comprehensive Income

As at 30 September 2021

	Notes	Year ended 30 September 2021 £m	Year ended 30 September 2020 £m
Profit / (loss) for the financial period		**5.8**	**(15.9)**
Re-measurement of defined benefit pension plan	24	2.6	(4.4)
Deferred tax thereon	18	(0.4)	0.7
Movement of pension scheme reimbursement asset	19	(1.0)	0.4
Deferred tax thereon	18	0.6	(0.1)
Total other comprehensive income		**1.8**	**(3.4)**
Total comprehensive income for the year		**7.6**	**(19.3)**

The results for the year ended 30 September 2021 relate entirely to continuing operations.

The notes on pages 72 to 127 form part of the financial statements of the Bank.

Balance Sheet

As at 30 September 2021

	Notes	30 September 2021 £m	30 September 2020 £m
Assets			
Cash and balances held at central banks		412.2	147.9
Government bonds	10	29.8	48.6
Debt securities	11	42.3	50.7
Loans and advances to credit institutions	12	45.9	105.2
Loans and advances to customers	13	1,061.5	930.8
Intangible assets	15	7.4	7.3
Property, plant & equipment	16	1.6	1.9
Investment properties	17	94.6	97.4
Deferred tax assets	18	11.5	9.5
Other assets	19	6.6	9.9
Total assets		**1,713.4**	**1,409.2**

	Notes	30 September 2021 £m	30 September 2020 £m
Liabilities			
Deposit from banks	20	145.0	87.5
Deposits from customers	21	1,381.0	1,071.4
Derivative financial instruments	22	14.7	82.0
Other liabilities	23	9.9	6.3
Pension liabilities	24	14.2	21.0
Total liabilities		**1,564.8**	**1,268.2**
Share capital and reserves			
Share capital	25	105.0	105.0
Other reserves		43.6	36.0
Total equity		**148.6**	**141.0**
Total equity and liabilities		**1,713.4**	**1,409.2**

These financial statements of the Bank were approved by the Board of directors on 6 December 2021 and were signed on its behalf by:

David Landen
Director

Statement of Changes in Equity

For the year ended 30 September 2021

	Called up share capital £m	Retained earnings £m	Pension reserve £m	Total £m
2021				
At beginning of period	105.0	50.4	(14.4)	141.0
Profit for the financial year	-	5.5	0.3	5.8
Other comprehensive income	-	-	1.8	1.8
Pension additional contribution	-	(1.6)	1.6	-
At end of financial period	**105.0**	**54.3**	**(10.7)**	**148.6**

	Called up share capital £m	Retained earnings £m	Pension reserve £m	Total £m
2020				
At beginning of period	105.0	66.7	(11.4)	160.3
Loss for the financial year	-	(16.3)	0.4	(15.9)
Other comprehensive income	-	-	(3.4)	(3.4)
At end of financial period	**105.0**	**50.4**	**(14.4)**	**141.0**

Notes to the Financial Statements

For the year ended 30 September 2021

1. Accounting policies

Basis of preparation

The financial statements of the Bank are prepared in accordance with Financial Reporting Standard 101 Reduced Disclosure Framework ("FRS 101").

The Bank is a privately-owned company incorporated and registered in England and Wales.

In preparing these financial statements, the Bank applies the recognition, measurement and disclosure requirements of International Financial Reporting Standards in conformity with the requirements of the Companies Act 2006, applicable to companies reporting under IFRS (Schedule 2 of The Large and Medium-sized Companies and Banks (Accounts and Reports) Regulations 2008) and has set out below where advantage of the FRS 101 disclosure exemptions has been taken.

The immediate parent undertaking of the Bank is Hodge Limited. The ultimate parent undertaking and controller is The Carlyle Trust (Jersey) Limited (incorporated in Jersey). Within the meaning of the Companies Act 2006, The Carlyle Trust Limited is the parent undertaking of the only group of undertakings for which group accounts are drawn up and of which the Bank is a member. The accounts of The Carlyle Trust Limited can be obtained from: The Registrar of Companies, Companies House, Crown Way, Cardiff, CF14 3UZ.

In these financial statements, the Bank has applied the exemptions available under FRS 101 in respect of the following disclosures:

- A Cash Flow Statement and related notes;
- Reconciliation between carrying amounts of investment properties at the beginning and at the end of the period;
- Disclosures in respect of transactions with members of a group;
- Disclosures in respect of the compensation of key management personnel and related parties.

The Bank proposes to continue to adopt the reduced disclosure framework of FRS 101 in its next financial statements.

The financial statements have been prepared on a going concern basis. The Board has considered the appropriateness of the going concern basis of preparation of the financial statements taking into account the Bank's current and projected performance, including consideration of projections incorporating the impact of the COVID-19 pandemic on the Bank's capital and funding position. As part of this assessment the Board considered:

- The impact on Bank's profits from an expected reduction in income from residential and commercial lending combined with increased credit impairment charges;
- The sufficiency of the Bank's capital base, which is expected to be sufficient to weather even a severe COVID-19 related downturn; and,
- The adequacy of the Bank's liquidity.

The Bank's forecasts and projections include scenario testing undertaken in accordance with the ICAAP and ILAAP, which are required by the Prudential Regulation Authority to demonstrate appropriate levels of capital and liquidity respectively under stressed conditions.

The directors confirm that they are satisfied that the Company will continue in business for a period of fifteen months to 31 December 2022. Consequently, the going concern basis continues to be appropriate in preparing the financial statements.

The accounting policies set out below have, unless otherwise stated, been applied consistently to all periods presented in these financial statements.

Standards and interpretations effective for the Company in these financial statements:

The Company has considered a number of amendments to published International Financial Reporting Standards and interpretations effective for the year ended 30 September 2021. They are either not relevant to the Bank or do not have a significant impact on the Bank's financial statements.

Standards and interpretations effective for the Company in future periods:

None of the standards issued by the IASB but not yet effective, are expected to have a material impact on the Bank's financial statements in future periods.

Summary of Significant Accounting Policies

Measurement convention

The Bank prepares its accounts under the historical cost convention, except for certain financial assets and liabilities held at fair value.

Interest receivable and interest payable

Interest income and expense are recognised in the Income Statement for all instruments measured at amortised cost using the effective interest rate method. The Bank estimates future cash flows considering all contractual terms of the financial instrument. The calculation includes all fees paid or received between parties to the contract that are an integral part of the effective interest rate, transaction costs and all other premiums or discounts. The net incremental transactional income/costs are amortised over the period to the contractual maturity date for commercial loans and based on the expected life of each loan for residential and buy-to-let portfolios.

1. Accounting policies (continued)

An allowance is made for prepayments for the residential portfolios, but no adjustment is made for the commercial and portfolio buy-to-let portfolios.

The gross carrying amount of a financial asset is the amortised cost of a financial asset before adjusting for any loss allowance. For credit-impaired financial assets i.e. Stage 3, a credit-adjusted effective interest rate is calculated using estimated future cash flows including loss allowance. The Bank does not currently hold any purchased or originated credit-impaired financial assets.

If the status of the asset subsequently recovers, the amount by which the provision has increased due to suspended interest is recognised as a reversal of impairment loss allowance rather than interest income. The reversal of impairment loss allowance will not be recognised until the reversal of the impairment is fulfilled.

Revenue Recognition

Investment income
Investment income consists of realised gains on financial assets and liabilities held at fair value through profit and loss ('FVTPL').

Realised gains and losses on financial assets and liabilities held at fair value represent the difference between the proceeds received, net of transaction costs, and the original cost.

Fees and commissions
Fee and commission income primarily relate to fees for originating and servicing mortgages on behalf of third-parties. Fee income is recognised when performance obligations attached to the fee or commission have been satisfied.

Financial instruments

Recognition
Financial assets and liabilities are recognised when the Bank becomes a party to the contractual provisions of the instrument. Purchases and sales of financial assets are recognised on the date in which they are settled.

Financial assets
The Bank has classified its financial assets as follows:

- Amortised cost: Cash and balances held with central bank, Residential, Portfolio buy-to-let and Commercial loans, Loans and advances to credit institutions, Government bonds, Debt securities and Other assets. These assets are held within a business model whose objective is to hold assets to collect contractual cash flows and the contractual terms of the loans are solely payments of principal and interest on the principal amount outstanding.
- FVTPL: Lifetime mortgages including Retirement and Equity release mortgages are classified as FVTPL due to the existence of an embedded derivative in the form of a 'No negative equity guarantee' ('NNEG') which forms part of the terms and conditions applicable to these products. To classify financial assets the Bank performs two assessments to evaluate the business model in which financial assets are managed and their cash flow characteristics.

The 'business model assessment' is performed at a portfolio level and determines whether the Bank's objective is to generate cash flows from collecting contractual cash flows, or by both collecting contractual cash flows and selling financial assets.

The assessment of cash flow characteristics determines whether the contractual cash flows of the financial asset are solely payments of principal and interest on the principal amount outstanding ('SPPI'). The SPPI test is performed at an instrument level based on the contractual terms of the instrument at initial recognition. For the purposes of the SPPI test, principal is defined as the fair value of the financial asset at initial recognition. Interest is defined as consideration for the time value of money and credit risk associated with the principal amount outstanding and for other basic lending risks and costs (e.g. liquidity risk and administrative costs), as well as a reasonable profit margin.

A financial asset is classified as measured at amortised cost if it meets both of the following conditions and is not designated as at FVTPL:

- It is held within a business model whose objective is to hold assets to collect contractual cash flows; and
- Its contractual terms give rise on specified dates to cash flows that are SPPI.

The Bank does not hold any financial instruments that are classified and measured at fair value through other comprehensive income, accordingly all financial assets not classified as measured at amortised cost are classified as FVTPL.

On initial recognition, the Bank may irrevocably designate a financial asset as FVTPL if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Financial liabilities

The Bank has classified its financial liabilities as follows:

- Amortised cost: Deposits from banks, Deposits from customers and Other liabilities.
- FVTPL: Derivatives.

De-recognition of financial assets and financial liabilities

(i) Financial assets
Financial assets are de-recognised when:

- The rights to receive cash flows from the asset have expired;
- The Bank has transferred its rights to receive cash flows or has assumed an obligation to pay the received cash flows in full without material delay; and either
- The Bank has transferred substantially all the risks and rewards of the asset; or

1. Accounting policies (continued)

- The Bank has neither transferred nor retained substantially all the risks and rewards of the asset but has transferred control of the asset.

Where an existing financial asset is replaced by another to the same customer on substantially different terms, or the terms of an existing facility are substantially modified, such an exchange or modification is treated as a de-recognition of the original asset and the recognition of a new asset.

(ii) Financial liabilities
Financial liabilities are de-recognised when the obligation is discharged, cancelled or has expired.

Fair value of financial instruments
On initial recognition, the best evidence of the fair value of a financial instrument is normally transaction price (i.e. the fair value of the consideration given or received). If the Bank determines that the fair value on initial recognition differs from the transaction price, the Bank accounts for such differences as follows:

- If fair value is evidenced by a quoted price in an active market for an identical asset or liability or based on a valuation technique that uses only data from observable markets, then the difference is recognised in the Income Statement on initial recognition (i.e. day 1 profit or loss);
- In all other cases, the fair value will be adjusted to bring it in line with the transaction price (i.e. day 1 profit or loss will be deferred by including it in the initial carrying amount of the asset or liability). Subsequently, the deferred gain or loss will be released to the Income Statement on an appropriate basis over the life of the instrument but no later than when the valuation is wholly supported by observable market data or the transaction is closed out.

The Bank uses a fair value hierarchy that categorises financial instruments into three different levels as detailed in note 27. Levels are reviewed at each reporting date and this determines whether transfers between levels are required.

Equity release and retirement mortgages
On initial recognition, the fair value of equity release and retirement mortgages is calculated by discounting the future expected cash flows at swap rates together with an allowance for illiquidity. The illiquidity spread is informed by examining the pricing of new originations amongst other market participants, creating a market consistent discount rate for the asset.

For equity release mortgages, if the difference between the fair value at transaction date and the transaction price is a gain, it is not recognised but deferred. This difference will be a short-lived effect and is deferred over one year and recognised uniformly over this period into the Income Statement. If the difference between the fair value and the transaction price is a loss upon initial recognition, it is expensed to the Income Statement.

On subsequent measurement, the value of retirement mortgages is calculated by projecting the cash flows expected to be generated by the portfolio on redemption, allowing for credit losses caused by the no-negative equity guarantee using a variant of the Black Scholes option pricing method. These cash flows are then discounted at the swap yield plus a margin to reflect the illiquidity of retirement mortgage assets, as described above. An allowance for possible early redemption of the retirement mortgages has been determined by reference to historical rates of lapse within the portfolio.

Embedded derivatives
The NNEG is an embedded derivative. The Company does not separate the NNEG embedded derivative from the host instrument. The fair value of lifetime mortgages takes into account an explicit provision in respect of the NNEG. Further details are disclosed in note 27(d).

Measurement of Expected Credit Loss (ECL)
Impairment of financial assets is calculated using a forward looking ECL model. The Bank records an allowance for ECLs ('loss allowance') for all financial assets not held at FVTPL.

Measurement of ECLs depends on the 'stage' of the financial asset, based on changes in credit risk occurring since initial recognition, as described below:

- Stage 1: when a financial asset is first recognised it is assigned to Stage 1 and a 12-month ECL is recognised. If there is no significant increase in credit risk from initial recognition the financial asset remains in Stage 1.
- Stage 2: if there is a significant increase in credit risk from initial recognition a financial asset it is moved to Stage 2 and a lifetime ECL is recognised.
- Stage 3: when there is objective evidence of impairment and the financial asset is considered to be in default, it is moved to Stage 3 and a lifetime ECL is recognised.

A 12-month ECL is defined as the portion of lifetime ECL that will result if a default occurs in the 12-months after the reporting date, weighted by the probability of that default occurring.

A lifetime ECL is defined as ECLs that result from all possible default events over the expected behavioural life of a financial instrument.

For loan commitments, where the loan commitment relates to the undrawn component of a facility, it is assigned to the same stage as the drawn component of the facility. For pipeline loans, the loan commitment is assigned to Stage 1.

If the contractual cash flows on a financial asset have been renegotiated or modified and the financial asset was not derecognised, an assessment is made to consider whether there has been a significant increase in the credit risk of the financial instrument.

Significant increase in credit risk
The Bank applies a series of quantitative, qualitative and backstop criteria to determine if there has been a significant increase in credit risk:

- Quantitative criteria: this is based on a doubling of the probability of default plus 45bps since origination for the commercial and portfolio buy-to-let exposures and a deterioration in a customer's credit score of greater than or equal to 160 points

1. Accounting policies (continued)

for residential mortgages. The quantitative criteria for which our commercial, portfolio buy-to-let and residential mortgages are annually reviewed by our credit risk teams.

- Qualitative criteria: this includes the observation of specific events such as short-term forbearance, payment cancellation, historical arrears or extension to customer terms.
- Backstop criteria: IFRS 9 includes a backstop that 30-days past due is an indicator of a significant increase in credit risk. The Bank considers 30-days past due to be an appropriate backstop measure and does not rebut this presumption. The granting of a short-term payment holiday of up to 60-days during the Covid-19 outbreak does not by itself represent a significant increase in credit risk.

Definition of default and credit-impaired assets
The Bank's definition of default is fully aligned with the definition of credit-impaired. The Bank applies both a qualitative and quantitative criterion to determine if an account meets the definition of default. These criteria include:

- When the borrower is more than 90-days past due; and
- Qualitative factors to comply with the internal rating systems risk grading approach adopted by the Bank.

Inputs into the assessment of whether a financial instrument is in default and their significance may vary over time to reflect changes in circumstances.

Presentation of loss allowances in the Balance Sheet
Loss allowances for financial assets measured at amortised cost are presented as a deduction from the gross carrying amount of the financial asset.

Write-offs
Loans and debt securities are written off (either partially or in full) when there is no realistic prospect of recovery.

Hedge accounting
The Bank has elected to continue to apply the hedge accounting requirements of IAS 39. All derivatives entered into by the Bank are for the purposes of providing an economic hedge. Where the criteria set out in IAS 39 are met, the Bank uses hedge accounting and designates the hedging derivative as hedging fair value risks.

At inception of the hedge relationship, the Bank formally documents the relationship between the hedged item and the hedging instrument, including the nature of the risk, the risk management objective and strategy for undertaking the hedge and the method that will be used to assess the effectiveness of the hedging relationship at inception and on an ongoing basis.

At each hedge effectiveness assessment date, a hedge relationship must be expected to be highly effective on a prospective basis and demonstrate that it was effective (retrospective effectiveness) for the designated period in order to qualify for hedge accounting. A formal assessment is undertaken by comparing the hedging instrument's effectiveness in offsetting the changes in fair value or cash flows attributable to the hedged risk in the hedged item, both at inception and at each quarter end on an ongoing basis. A hedge is expected to be highly effective if the changes in fair value or cash flows attributable to the hedged risk during the period for which the hedge is designated were offset by the hedging instrument in a range of 80% to 125% and were expected to achieve such offset in future periods.

Hedge ineffectiveness is recognised in the Income Statement in other fair value gains and losses. For situations where the hedged item is a forecast transaction, the Bank also assesses whether the transaction is highly probable and presents an exposure to variations in cash flows that could ultimately affect the Income Statement.

Derivatives are introduced into the portfolio at inception and therefore this prevents a large gain or loss on the hedged item as the derivative is introduced into the fair value macro hedge portfolio. Any gain or loss is amortised over the period to the date of maturity of the derivative. If a derivative no longer meets the criteria for hedge accounting, the cumulative fair value hedging adjustment is amortised over the period to maturity of the previously designated hedge relationship. If the underlying hedged item is sold or repaid, the unamortised fair value adjustment is recognised in the Income Statement.

Intangible assets
Where software costs are capitalised, they are amortised using the straight-line method over their estimated useful lives which is three to ten years. The amortisation periods used are reviewed annually. Costs associated with maintaining software are expensed as they are incurred. Amortisation is charged to its own line in the Income Statement.

Intangible assets have finite lives and are assessed for indicators of impairment at each Balance Sheet date.

An intangible asset is impaired where there is objective evidence that, as a result of one or more events that occurred after initial recognition, the estimated recoverable value of the asset has been reduced. The recoverable amount of the intangible assets is deemed to be its value in use. If there is objective evidence of impairment, an impairment loss is recognised in the Income Statement.

Property, plant and equipment
Property, plant and equipment is stated at cost less accumulated depreciation and any accumulated impairment losses.

Depreciation is provided on a straight-line basis over the anticipated useful lives as follows:

- Fixtures, fittings and equipment 3 - 10 years

Investment properties – reversionary interests in properties
Reversionary interests in properties are included in the financial statements initially at cost and subsequently at fair value, with any change therein recognised in the Income Statement within other fair value gains and losses on investments.

The current market value of the underlying property is taken as the last formal valuation of the property on a vacant possession basis, modified by

1. Accounting policies (continued)

the change in the quarterly Nationwide Regional House Price Index, adjusted down by an annual underperformance assumption.

A further deduction is made from the value to reflect the expected sale expenses and a delay factor between death and sale of the property.

Investment properties are derecognised either when they have been disposed of, or when the investment property is permanently withdrawn from use and no future economic benefit is expected from its disposal. Any gains or losses on derecognition are recognised in the Income Statement in the year of disposal within investment income.

Taxation including deferred tax
Corporation tax on profits for the year comprises current and deferred taxation.

Current tax assets and liabilities are measured at the amount expected to be recovered from or paid to the taxation authorities, based on tax rates and laws that are enacted or substantively enacted by the Balance Sheet date. Where group relief is received or surrendered from or to a group company, the corresponding liability or asset is settled in full.

Deferred tax is recognised on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the financial statements of the Bank. Deferred tax assets are recognised only to the extent that it is probable that future taxable profits will be available against which the deductible temporary differences, carried forward tax credits or tax losses can be utilised.

Deferred tax assets and liabilities are measured on a non-discounted basis at the tax rates that are expected to apply when the related asset is realised, or liability settled based on the tax rates and laws enacted or substantively enacted at the Balance Sheet date.

Corporation tax is charged directly to the Income Statement.

Employee benefits

i) Pensions
The Bank has two pension schemes, a defined benefit scheme and a defined contribution scheme.

Defined Benefit Pension
The Bank operated a defined benefit pension scheme which is now closed to new entrants and to further accrual. The Bank participates in The Carlyle (1972) Pension and Life Assurance Scheme, a defined benefits scheme operated by The Carlyle Trust Limited. The assets of the scheme are held separately from those of the Bank.

The Bank's net obligation under the defined benefit pension scheme is assessed annually by an independent qualified actuary. The net obligation is calculated as the difference between the fair value of the scheme's assets and the amount of future entitlements earned by scheme members from service in the current and prior periods, discounted back to present values using a rate based on an index of long-dated AA rated corporate bonds using the projected unit method. This calculation allows the net obligation of the scheme to be expressed as either a surplus or deficit, which is recognised as either an asset or liability respectively in the Bank's accounts at the Balance Sheet date.

Defined Contribution Scheme
The Bank introduced a defined contribution scheme during the year, replacing the defined benefit scheme. A defined contribution scheme is one into which the Bank and the employee pay fixed contributions, without any obligation to pay further contributions. Payments into the defined contribution scheme are charged to the Income Statement as they become payable in accordance with the rules of the scheme.

ii) Reimbursement asset/ liability on pension deficit
The Bank has recognised a reimbursement liability to its parent company in respect of its pension scheme deficit which relates to retired employees that were contracted to the Bank's ultimate parent, The Carlyle Trust Limited ('TCT') (note 24). The movement in the reimbursement asset/ liability each year is recognised in the Income Statement to the extent that the reimbursement relates to a charge or a gain in the Bank's Income Statement. The defined benefit pension scheme liabilities is split between TCT and the Bank based on the split of scheme members by employer. The defined benefit pension scheme assets have been split in proportion to the scheme's liabilities at 30 September 2020. Any payments made into the scheme from this date are allocated to the assets of the employer making the payment. The reimbursement asset/ liability represents the value of TCT's defined benefit pension scheme's assets less its share of the scheme's liabilities.

2. Judgement in applying accounting policies and critical accounting estimates

The Bank has to make judgements in applying its accounting policies which affect the amounts recognised in the financial statements of the Bank. In addition, estimates and assumptions are made that could affect the reported amounts of assets and liabilities within the following financial year. The most significant areas where judgement and estimates are made are as follows:

Judgements

Fair values of financial instruments
The Bank uses widely recognised valuation models for determining the fair value of common and simple financial instruments, such as interest rate swaps that use only observable market data. Further analysis can be found in note 27.

The availability of observable market prices and model inputs reduces the need for management judgement and also reduces the uncertainty associated with determining fair values. The availability of observable market prices and inputs varies depending on the products and markets and is prone to changes based on specific events and general conditions in the financial markets.

Where observable market data is unavailable, unobservable inputs are used in the actuarial valuation models to value equity release and retirement mortgages held at FVTPL. The key judgements and assumptions used, and the related sensitivities are outlined in note 27.

Estimates and assumptions

Impairment losses on loans and advances to customers
IFRS 9 has a single impairment model that applies to all financial instruments in its scope. Under this model, an entity must recognise either a 12-month or lifetime expected credit loss. ECLs are the present value of all cash shortfalls over the expected life of the financial instrument. The key assumptions used, and the related sensitives, are outlined in note 28.

Value of reversionary investment properties
There is significant judgement applied in setting the assumptions used in calculating the fair value of reversionary interests in property. Further information on the following assumptions is provided in note 17.

- Property prices
- Mortality or entry into long term care
- Expense assumption
- Discount rate

Pension scheme assumptions
Estimation uncertainty surrounds the measurement of the pension scheme liabilities. The assumptions used as part of the valuation include the rate of salary increase, the discount rate applied to scheme liabilities and inflation. The key assumptions used are disclosed in note 24.

Value of equity release and retirement mortgages including the value of the NNEG
There is significant judgement applied in setting the assumptions used in calculating the fair value of lifetime mortgages and the liability arising from the no-negative equity guarantee. Further information on the following assumptions is provided in note 27(d).

- Mortality or entry into long term care
- Lapses
- Expense assumption
- Discount rate
- Property prices

Change in accounting estimates
There is significant judgement in the methodologies and assumptions applied in estimating the fair value of lifetime mortgages and reversions. The methodologies and assumptions contain unobservable inputs resulting in the fair value being classified as a Level 3 estimate within the IFRS 13 fair value hierarchy. Changes have been made during the period to the methodology used to discount the anticipated cash flows associated with the reversion and lifetime mortgage portfolios. The change in methodology results in a valuation approach that is more consistent with the approach used by many other financial institutions that hold these types of assets. The impact of these changes is disclosed within note 27 and are recognised prospectively as a change in accounting estimate.

3. Segmental information

The Board is the Bank's chief operating decision-maker (CODM). Management has determined the operating segments based on information reviewed by the Board for the purposes of allocating resources and assessing performance.

Year ended 30 September 2021	Commercial £m	Residential £m	Portfolio Buy-to-Let £m	Other £m	Total £m
Interest receivable and similar income	13.1	23.4	2.6	0.5	39.6
Interest payable and similar charges	(4.7)	(15.6)	(1.4)	(0.3)	(22.0)
Fees and commissions receivable	0.3	1.1	-	1.1	2.5
Investment income	-	6.0	-	-	6.0
Other operating income	-	-	-	0.1	0.1
Administrative expenses	(5.3)	(14.4)	(1.5)	(4.7)	(25.9)
Depreciation and amortisation	-	(0.9)	-	(1.5)	(2.4)
Impairment losses on loans and advances to customers	0.5	(0.1)	(0.4)	-	-
Operating loss	**3.9**	**(0.5)**	**(0.7)**	**(4.8)**	**(2.1)**

11-month period ended 30 September 2020	Commercial £m	Residential £m	Portfolio Buy-to-Let £m	Other £m	Total £m
Interest receivable and similar income	15.7	18.0	1.8	2.9	38.4
Interest payable and similar charges	(6.1)	(14.9)	(1.0)	(0.8)	(22.8)
Fees and commissions receivable	0.3	1.3	-	0.2	1.8
Investment income	-	3.5	-	-	3.5
Administrative expenses	(5.4)	(11.6)	(1.2)	(4.1)	(22.3)
Depreciation and amortisation	-	(0.6)	-	(1.2)	(1.8)
Impairment losses on loans and advances to customers	(5.4)	0.1	(0.1)	-	(5.4)
Operating loss	**(0.9)**	**(4.2)**	**(0.5)**	**(3.0)**	**(8.6)**

Total assets by business segments	2021 £m	2020 £m
Commercial	233.9	290.5
Residential	852.3	671.2
Portfolio Buy-to-Let	70.5	63.1
Other	556.7	384.4
	1,713.4	**1,409.2**

4. Interest receivable and similar income

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Interest income calculated using EIR method		
Loans and advances to customers	38.8	36.1
Loans and advances to credit institutions	0.3	1.0
Interest on government bonds & debt securities	0.5	1.3
	39.6	**38.4**

5. Interest payable and similar charges

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
On customer accounts	13.8	14.5
On defined benefit pension scheme	0.3	0.3
On term funding scheme	0.1	0.2
On derivative financial instruments	7.8	7.8
	22.0	**22.8**

6. Administrative expenses

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Staff costs		
Wages and salaries	14.5	10.6
Social security	1.4	1.2
Pension costs – defined benefit scheme (note 24)	1.4	3.0
Pension costs – defined contribution scheme	0.8	-
Pension curtailment gain (note 24)	(0.7)	-
	17.4	**14.8**
Other administrative expenses	8.5	7.5
	25.9	**22.3**

6. Administrative expenses (continued)

Directors and employees
The average number of employees of the Bank during the period was as follows:

	Year ended 30 September 2021	11-months ended 30 September 2020
Provision of finance and banking	321	277
	321	**277**

Staff costs include remuneration in respect of directors as follows:

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Fees	0.4	0.3
Aggregate emoluments as executives	0.6	0.4
	1.0	**0.7**

The emoluments of the highest paid director, excluding pension contributions, were as follows:

	Year ended 30 September 2021	11-months ended 30 September 2020
Aggregate emoluments	240	189
	240	**189**

The pension accrued for the highest paid director was £14,104 *(2020: £36,817)*.

Retirement benefits accrued to two *(2020: three)* directors in the defined benefit scheme.

7. Other fair value gain/ (losses)

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Movement in fair value of derivatives (note 22)	22.0	(4.6)
Movement in fair value of equity release and retirement mortgages	(11.5)	(9.6)
Reversal of unrealised gains on disposal of investment properties	(6.1)	(2.9)
Movement in fair value of investment properties (note 17)	6.6	4.6
Movement in fair value of hedged items attributable to hedged risk	0.3	(4.2)
	11.3	**(16.7)**

8. Profit / (loss) on ordinary activities before taxation

	Year ended 30 September 2021 £000	11-months ended 30 September 2020 £000
Profit / (loss) on ordinary activities before taxation is stated after charging:		
Remuneration of the auditor and its associates		
Audit of these financial statements of the Bank	298	177
Audit of pension scheme	11	11
Impairment provision expense (note 14)	-	5,435
Amortisation (note 15)	1,855	1,308
Depreciation (note 16)	510	452

9. Tax on profit

	Year ended 30 September 2021 £m		11-months ended 30 September 2020 £m	
Analysis of charge in the financial period				
UK corporation tax				
Current tax on income for the year	(0.1)		(2.4)	
Prior period adjustment	(-)		(0.5)	
Total current tax		**(0.1)**		**(2.9)**
Deferred tax				
Origination/reversal of timing differences:				
Current period	1.4		(1.6)	
Prior period adjustment	(0.4)		0.1	
Effect of tax rate change on opening balance	(3.0)		(0.8)	
Total deferred tax (note 18)		**(2.0)**		**(2.3)**
Tax credit on profit on ordinary activities		**(2.1)**		**(5.2)**

The total tax charge for the period is lower than 19% *(2020: lower than 19%)* the blended rate of corporation tax in the UK. The differences are explained below.

	Year ended 30 September 2021 £m	11-months ended 30 September 2020 £m
Total tax reconciliation		
Profit / (loss) on ordinary activities before tax	3.7	(21.1)
Current tax at 19.00% (2020: 19.00%)	**0.7**	**(4.0)**
Expenses not deductible for tax purposes	0.6	-
Rate differences	(3.0)	(0.8)
Adjustments in respect of previous years	(0.4)	(0.4)
Total tax credit (see above)	**(2.1)**	**(5.2)**

In the current period the UK government announced that from 1 April 2023 the corporation tax rate will increase from 19% to 25%. The closing deferred tax assets and liabilities have been calculated at 25% and accordingly a rate change adjustment has arisen as the opening deferred tax had been calculated taking into account the previously enacted rate of 19%.

10. Government bonds

	2021	2020
Government bonds – at amortised cost	29.8	48.6
	29.8	**48.6**

The movement in government bonds is summarised as follows:

	2021 £m	2020 £m
At start of period	48.6	25.1
Additions	-	74.2
Redemptions and interest received	(18.1)	(39.8)
Disposals due to restructuring exercise	-	(7.6)
(Loss)/gain from hedge accounting – Income Statement	-	(3.3)
Premium/ discount unwind	(0.7)	-
At end of financial period	**29.8**	**48.6**

Of this amount, £nil (2020: £12.0m) has been pledged as collateral under the Term Funding Scheme ('TFS').

11. Debt securities

	2021 £m	2020 £m
Debt securities – at amortised cost	42.3	50.7
	42.3	**50.7**

	2021 £m	2020 £m
At start of period	50.7	57.0
Additions	-	5.5
Redemptions and interest received	(8.3)	(5.8)
Disposals due to restructuring exercise	-	(5.4)
Loss from hedge accounting - Income Statement	(0.1)	(0.6)
At end of financial period	**42.3**	**50.7**

Of this amount £nil (2020: £32.8m) has been pledged as collateral under the TFS.

12. Loans and advances to credit institutions

	2021 £m	2020 £m
Repayable on demand	23.4	19.1
Collateral held by swap counterparties	22.5	86.1
	45.9	**105.2**

The collateral is pledged against the market value of derivative instruments and comprises interest-bearing cash deposits (note 22). Collateral that has been pledged and held is not restricted and is returned at the end of the contract. There are no provisions held in respect of loans and advances to credit institutions (2020: £nil).

13. Loans and advances to customers

	2021 £m	2020 £m
Loans and advances – classified at amortised cost		
Commercial	233.9	290.5
Residential	679.0	347.0
Portfolio Buy-to-Let	70.5	63.1
	983.4	**700.6**
Amounts owed from parent and fellow subsidiaries	0.4	3.1
Fair value adjustment for hedged risk	(1.0)	0.3
Loans and advances (equity release and retirement) – classified as FVTPL - see note 27	78.7	226.8
	1,061.5	**930.8**

Of this amount £190.4m (2020: £68.6m) has been pledged as collateral under the TFS. Collateral that has been pledged is restricted. During the year the Bank disposed of a portfolio of equity release mortgages for strategic purposes leading to a £5.5 million loss on disposal.

The amounts owed from parent is a loan due from The Carlyle Trust Limited and accrues a market rate of interest.

	2021 £m	2020 £m
Loans and advances to customers at amortised cost		
Gross balances	989.9	709.3
Less: Provision for impairment	(8.4)	(7.9)
Less: Loan fee deferral	1.9	(0.8)
Net balance	**983.4**	**700.6**

14. Impairment provisions on loans and advances to customers

IFRS 9	Stage 1 £m	Stage 2 £m	Stage 3 £m	Stage 4 £m
2021				
At start of period	1.5	1.6	4.8	7.9
Utilised in period	-	-	-	-
Income Statement				
Charge for loan impairment	(0.2)	0.4	0.1	0.3
Interest reduction for credit-impaired financial assets	-	-	0.2	0.2
At 30 September 2021	**1.3**	**2.0**	**5.1**	**8.4**

During the year, the Bank has recovered £0.3m (2020: £nil) on a bad debt previously written off, this recovery has been recognised within the 'charge for loan impairment' line on the face of the Income Statement, reducing the charge for loan impairment to £nil (2020: £5.4m).

IFRS 9	Stage 1 £m	Stage 2 £m	Stage 3 £m	Stage 4 £m
2020				
At start of period	2.4	0.1	7.3	9.8
Utilised in the period	-	-	(7.3)	(7.3)
Income Statement				
Charge for loan impairment	(0.9)	1.5	4.8	5.4
At 30 September 2020	**1.5**	**1.6**	**4.8**	**7.9**

The impact of modifications to contractual cash flows that has not resulted in derecognition is immaterial in the year.

For further details on loans and advances to customers refer to note 28.

15. Intangible assets

	Computer software	
	2021	2020
	£m	£m
Cost:		
At start of period	10.1	7.4
Disposals	-	(0.1)
Additions	1.9	2.8
At end of financial period	**12.0**	**10.1**
Amortisation:		
At start of period	(2.8)	(1.6)
Disposals	-	0.1
Amortisation	(1.8)	(1.3)
At end of financial period	**(4.6)**	**(2.8)**
Net book value:		
At end of financial period	**7.4**	**7.3**

£1.5m (2020: £2.3m) of expenditure relating to intangible projects was expensed during the year as it did not meet the development criteria of IAS 38 and has therefore been expensed as incurred.

16. Property, plant and equipment

	Fixtures, fittings and equipment	
	2021	2020
	£m	£m
Cost:		
At start of period	3.5	3.0
Additions	0.2	0.5
Disposals	(0.8)	-
At 30 September 2021	**2.9**	**3.5**
Depreciation:		
At start of period	(1.6)	(1.1)
Depreciation	(0.5)	(0.5)
Disposals	0.8	-
At 30 September 2021	**(1.3)**	**(1.6)**
Net book value:		
At 30 September 2021	**1.6**	**1.9**

17. Investment properties

	Reversionary Interests £m
At start of period	97.4
Disposals	(9.4)
Fair value adjustments	6.6
At 30 September 2021	**94.6**

The historical cost of the reversionary interest in properties is £38.1m at 30 September 2021 (2020: £41.3m).

Reversionary interests are categorised as Level 3 in the fair value hierarchy. There were no transfers into or out of Level 3 in the year.

Reversionary interests - principal assumptions
All gains and losses arising from reversionary interests are largely dependent on the longevity of the tenant. Principal assumptions underlying the calculation of reversionary interests include the following:

Mortality or entry into long term care
This is based on the expected death or entry into long term care of the tenant or the last remaining tenant in relation to a joint contract. Mortality assumptions have been derived by reference to the PCMA00/PCFA00 mortality tables and include an allowance for mortality improvements. This table is adjusted from 2000 to 31 December 2018 for mortality improvements based on the CMI 2017 mortality projection model. The table is further adjusted from 31 December 2018 to 31 December 2020 using the CMI 2018 mortality projection model, and mortality improvements from 31 December 2020 onwards are based on the CMI 2018 mortality projections model. Finally, the mortality tables are further adjusted to reflect recent mortality experience by multiplying the mortality rates by a percentage factor. Given that the CMI 2018, 2019 and 2020 mortality projection models produce similar life expectancies, the mortality improvement assumptions for the 2021 year-end is unchanged; in particular, in light of the high level of uncertainty associated with the impact of COVID-19 on mortality improvements over the medium to long-term we have assumed no impact of COVID-19 on future mortality improvements, but this will continue to be monitored.

Early redemptions are expected to be very infrequent, and therefore the voluntary redemptions rate is included in the mortality assumption.

Expenses
Assumptions for future policy expense levels are based on the Bank's recent expense analysis. Expenses are modelled as an amount per policy per annum that incorporates an annual inflation rate allowance of 4.59% p.a. as at 30 September 2021 (2020: 4.09% p.a.). This rate is equal to the market implied rate of RPI inflation (appropriate for the average duration of the reversion portfolio) plus an allowance for expenses increasing faster than the market expectation of prices.

Discount rate
The discount rate applied to the reversion cash flows comprises two parts: a risk-free yield curve plus a spread referred to as the illiquidity spread.

The risk-free yield curve is based on the PRA's Solvency II curve methodology, which uses SONIA swap rates. An internal tool developed by Milliman is used to derive the expected PRA curve for use in each month's valuation; this is then validated against the actual PRA curve when it is published.

The average discount rate for the portfolio (assumed to be the 8-year point on the yield curve based on the expected average duration) at 30 September 2021 was 3.03% - including an illiquidity spread of 2.17% (2020: 2.27%).

Property prices
The value of a property is based on the value at the last survey increased to the current valuation date using the Nationwide Regional House Price Index. This is then adjusted down by a 10% haircut to reflect the expectation that property prices underperform the house price index due to the older age of the policyholders and a disincentive to maintain the property when it is subject to a reversion. For properties that have been subject to a physical or drive-by valuation, the 10% haircut will not be applied as these valuations will already reflect the condition of the property. No future property price inflation is assumed beyond the valuation date.

17. Investment properties (continued)

Sensitivity analysis
Changes to unobservable inputs used in the valuation technique could give rise to significant changes in the fair value of the assets. The Bank has estimated the net decrease in profit before tax for the period arising from changes to these inputs as follows:

	Reversionary Interests			
	Delay in mortality or entry into long term care - 10%	Discount rate +1%	Expenses +10%	Property prices -10%
	£m	£m	£m	£m
At 30 September 2021	**(1.5)**	**(5.3)**	**(0.4)**	**(8.6)**
At 30 September 2020	(1.1)	(2.1)	(0.2)	(8.7)

The sensitivity factors are applied via actuarial models. The analysis has been prepared for a change in each variable with other assumptions remaining constant. In reality, such an occurrence is unlikely due to correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear and larger or smaller impacts cannot be interpolated or extrapolated from these results.

18. Deferred tax

	2021 £m	2020 £m
At start of period	9.5	6.6
Credit to the Income Statement – current period	1.4	2.3
Credit to the Income Statement – prior period	0.4	-
Credit to the Statement of Other Comprehensive Income – reimbursement asset	0.6	(0.1)
Debit to the Statement of Other Comprehensive Income – defined benefit pension scheme	(0.4)	0.7
At end of financial period	**11.5**	**9.5**

Deferred tax assets and liabilities are attributable to the following items:

	2021 £m	2020 £m
Accelerated capital allowances	(0.5)	(0.3)
Other timing differences	4.5	4.2
Timing differences on reimbursement asset	-	(0.6)
Defined benefit pension scheme	3.6	4.0
Tax losses	3.9	2.2
At end of financial period	**11.5**	**9.5**

19. Other assets

	2021 £m	2020 £m
Prepayments and accrued income	2.6	2.3
Pension reimbursement asset	-	3.3
Corporation tax debtor	0.8	1.2
Group relief debtor	0.1	2.9
Other assets	3.1	0.2
At end of financial period	**6.6**	**9.9**

20. Deposits from banks

	2021 £m	2020 £m
Repurchase agreement	-	2.5
Term Funding Scheme	145.0	85.0
	145.0	**87.5**

21. Deposits from customers

	2021 £m	2020 £m
Deposit from customers	1,248.5	1,066.6
Amounts owed to parent and fellow subsidiaries	132.7	4.4
Fair value adjustment for hedged risk	(0.2)	0.4
	1,381.0	**1,071.4**

The amounts owed to parent and fellow subsidiaries are deposit accounts which accrue a market rate of interest.

22. Derivative financial instruments

Interest rate swaps are used by the Bank for hedging purposes. These are commitments to exchange one set of cash flows for another. No exchange of principal takes place.

	Contract/notional amount		Fair value	
	2021	2020	2021	2020
	£m	£m	£m	£m
Derivative liabilities held for hedging purposes and designated fair value hedges:				
Interest rate swaps	155.2	264.8	(15.8)	(81.9)
Derivatives held in fair value hedges	164.0	152.7	1.1	(0.1)
Total recognised derivative liabilities	**319.2**	**417.5**	**(14.7)**	**(82.0)**

The following table describes the types of derivatives used, the related risks and the activities against which the derivative financial instruments are used to hedge.

Type of Hedge	Risk	Activity
Interest rate swap	Sensitivity to changes in interest rates	Fixed rate savings products, Fixed rate residential mortgages, Fixed rate debt securities, Fixed rate government bonds and Fixed rate commercial loans.

At 30 September 2021, the fixed interest rates vary from 0.0% to 4.9% (2020: 0.2% to 5.4%), the floating rates are both LIBOR and SONIA. Gains and losses recognised on interest rate swap contracts are credited to the Income Statement.

	2021	2020
	£m	£m
Movement in fair value of interest rate swaps	22.0	(4.6)
	22.0	**(4.6)**

22. Derivative financial instruments (continued)

The Bank agreed to exit a number of interest rate swaps during the year which were held at fair value of £45.0m (2020: £0.7m), £0.3m (2020: £nil) profit or loss was incurred on disposal.

The amounts relating to items designated as hedged items were as follows:

	2021		2020	
	Book Value £m	Hedged Fair Value £m	Book Value £m	Hedged Fair Value £m
Government bonds	29.8	-	48.6	-
Debt securities	42.3	-	50.7	-
Loans advances to customers	983.4	(1.0)	702.3	0.4
Deposits from customers	(1,248.4)	0.2	(1,066.6)	(0.4)
		(0.8)		**-**

Offsetting
In accordance with IAS32 Financial Instruments; the Bank reports derivative financial instruments on a net basis as there is a legally enforceable right to set-off the recognised amounts and there is an intention to settle on a net basis, or to realise the asset and settle the liability simultaneously. A table is provided below which demonstrates the amounts which have been offset in the Balance Sheet:

	Amounts subject to netting arrangements		
	Gross amounts £m	Amounts offset £m	Net amounts reported on Balance Sheet £m
2021			
Derivative financial assets	2.3	(2.3)	-
Impact on total assets	**2.3**	**(2.3)**	**-**
Derivative financial (liabilities)	(17.0)	2.3	(14.7)
Impact on total (liabilities)	**(17.0)**	**2.3**	**(14.7)**
2020			
Derivative financial assets	1.0	(1.0)	-
Impact on total assets	**1.0**	**(1.0)**	**-**
Derivative financial (liabilities)	(83.0)	1.0	(82.0)
Impact on total (liabilities)	**(83.0)**	**1.0**	**(82.0)**

The collateral pledged against the market value of derivative instruments comprises interest bearing cash deposits, which are included in loans and advances to credit institutions (note 12).

23. Other liabilities

	2021 £m	2020 £m
Due within one year:		
Amounts owed in relation to mortgages administered for third parties	6.1	2.3
Other creditors	0.3	-
Other taxation and social security	0.5	0.1
Accruals	3.0	1.1
Amounts owed to fellow subsidiaries	-	2.8
	9.9	**6.3**

The amounts owed to fellow subsidiaries are repayable on demand and accrue no interest.

24. Pension scheme

The Carlyle Trust Limited group operates a defined benefit pension scheme for certain directors and employees, The Carlyle (1972) Pension and Life Assurance Scheme.

The assets of the scheme are administered by the Trustees and are held in a fund that is separate and independent of other group funds. The scheme was established with effect from 1972 and is fully approved under Chapter I Part XIV of the Income and Corporation Taxes Act 1988.

The scheme is subject to the funding legislation outlined in the Pensions Act 2004. This, together with documents issued by the Pensions Regulator, and Guidance Notes adopted by the Financial Reporting Council, sets out the framework for funding defined benefit occupational pension schemes in the UK.

The scheme typically exposes the Bank to actuarial risks such as investment risk, interest rate risk, mortality risk and longevity risk. A decrease in corporate bond yields, a rise in inflation or an increase in life expectancy would result in an increase to plan liabilities. This would detrimentally impact the Balance Sheet and may give rise to increased charges in future periods. The Bank has not changed its processes used to manage its risks from previous periods.

The weighted average duration of the defined pension obligation is 24 years (2020: 24 years).

Pension costs are assessed in accordance with the advice of a qualified, independent actuary using the projected unit method. The assumptions which have the most significant effect on the calculation are the long-term average investment return expected in future and the rate of future increases to benefits, both before and after retirement.

The benefit basis changed to a career average revalued earnings ("CARE") basis, from a final salary basis, with effect from 1 April 2005.

The calculations are based upon an assessment of the scheme's liabilities as at 30 September 2021. These have been based upon the results of the 1 April 2019 formal triennial valuation projected forward with allowance for benefit accrual and expected investment return. The next triennial valuation will be carried out on 1 April 2022.

The Bank's total expense for the year amounted to £1.0m (2020: £3.4m).The Bank's parent company, The Carlyle Trust Limited, reimbursed the Bank £0.0m (2020: £0.2m) for their share of the employer contribution expense. The Bank has agreed that it will aim to eliminate the pension scheme deficit over the next 10 years and additional contributions of £1.6m (2020: £0.9m) were paid into the scheme in the year ended 30 September 2021. The Carlyle Trust Limited agreed to make a one-off deficit reduction payment of £2.4m during the year which reduced the reimbursement asset held on the Balance Sheet of the Bank. Funding levels are monitored on an annual basis and the Bank has agreed to increase the contribution rate to 23.3% from 1 April 2019.

The IAS 19 valuation as at 30 September 2021 has been produced by a qualified independent actuary and is based on the results of the valuation as at 1 April 2019.

24. Pension scheme (continued)

Scheme assets and liabilities
The fair value of the scheme's assets, which are not intended to be realised in the short term and may be subject to significant change before they are realised, and the present value of the scheme's liabilities, which are derived from cash flow projections over long periods and thus inherently uncertain, were:

	2021 £m	2020 £m
Fair value of plan assets	37.9	30.3
Present value of defined benefit obligations	(52.1)	(51.3)
Deficit	**(14.2)**	**(21.0)**

Movements in fair value of plan assets

	2021 £m	2020 £m
Market value of assets at the beginning of the year	30.3	27.3
Interest income	0.5	0.5
Actuarial gain /(loss)	2.7	(0.4)
Member contributions	0.3	0.4
Employer contributions	5.2	3.3
Benefits paid	(1.1)	(0.8)
Market value of assets at the end of the period	**37.9**	**30.3**

Movements in present value of defined benefit obligations

	2021 £m	2020 £m
Present value of scheme liabilities at start of the period	51.3	43.9
Interest cost	0.8	0.8
Current service cost	1.4	3.0
Member contributions	0.3	0.4
Actuarial loss on defined benefit obligation of which:		
due to experience	(0.3)	-
due to demographic assumptions	-	0.9
due to financial assumptions	0.4	3.1
Benefits paid	(1.1)	(0.8)
Curtailments	(0.7)	-
Present value of scheme liabilities at end of the period	**52.1**	**51.3**

24. Pension scheme (continued)

Expense recognised in the Income Statement

	2021 £m	2020 £m
Current service cost – staff costs	1.4	3.0
Net interest expense – other finance costs	0.2	0.3
Curtailment gain	(0.7)	-
Other admin costs	0.2	0.1
	1.1	**3.4**

The total amount recognised in the Statement of Other Comprehensive Income in respect of actuarial gains and losses is a gain of £2.6m (2020: loss of £4.4m) before tax.

Cumulative losses reported in the Statement of Other Comprehensive Income since the date of transition to FRS 101 are losses of £10.7m (2020: losses of £14.4m) after deferred tax.

A curtailment gain of £0.7m was recognised in the Income Statement during the year as a result of the closure of the defined benefit scheme to further accrual.

Plan assets
The fair value of the plan assets and the return on those assets was as follows:

	Fair Value	
	2021 £m	2020 £m
Quoted equity investments	7.2	5.5
Diversified growth funds	7.6	18.5
Private investments	5.7	2.4
Bonds	7.6	1.8
LDI	8.7	-
Cash	1.1	2.1
Total market value of assets	**37.9**	**30.3**

The actual return on assets was £3.2m (2020: £0.1m).

Future contributions
The Bank expects to contribute approximately £1.6m (2020: £2.8m) to its defined benefit plan in the next financial year.

24. Pension scheme (continued)

Major assumptions
The major assumptions underpinning the defined benefit obligation are:

	2021 %	2020 %
Rate of increase in salaries	-	2.9
Rate of increase – RPI capped at 5.0% per annum	3.4	2.8
Rate of CARE revaluation	-	1.9
Discount rate applied to scheme liabilities	2.1	1.6
RPI inflation assumption	3.5	2.9

The assumptions relating to longevity underlying the pension liabilities at the Balance Sheet date are based on standard actuarial mortality tables and include an allowance for future improvements in longevity. The life expectancy of scheme members is as follows:

	2021	2020
Current pensioners age 65 – male	86.8	86.8
Current pensioners age 65 – female	89.1	89.1
Future pensioners age 65 (current age 45) - males	87.8	87.8
Future pensioners age 65 (current age 45) - females	90.3	90.2

Sensitivities
The Bank has to make assumptions on the discount rate, inflation and life expectancy when valuing the pension scheme liability. The sensitivity of the defined pension obligation to changes in the weighted principal assumptions is:

Impact on present value of obligation:	Change in assumption	Change in deficit £m
Discount rate	0.1%	1.3
Rate of inflation (RPI or CPI)	0.1%	0.9
Life expectancy	1 year	1.7

The sensitivity analyses above have been determined based on a method that extrapolates the impact on the defined benefit obligation as a result of reasonable changes in key assumptions occurring at the end of the reporting period. The sensitivity analyses are based on a change in a significant assumption, keeping all other assumptions constant. The sensitivity analyses may not be representative of an actual change in the defined benefit obligation as it is unlikely that changes in assumptions would occur in isolation of one another.

24. Pension scheme (continued)

History of the scheme Balance Sheet position

	2021 £m	2020 £m	2019 £m	Other £m	2017 £m
Fair value of plan assets	37.9	30.3	27.3	24.2	24.2
Present value of funded defined benefit obligations	(52.1)	(51.3)	(43.9)	(37.0)	(37.2)
Deficit	**(14.2)**	**(21.0)**	**(16.6)**	**(12.8)**	**(13.0)**

History of experience gains and losses

	2021	2020	2019	2018	2017
Difference between the expected and actual return on scheme assets:					
Amount	**£2.7m**	£(0.4)m	£0.6m	£(1.4)m	£0.1m
Percentage of year-end scheme assets	**7.1%**	1.3%	2.2%	(5.6)%	0.0%
Experience gains and losses on scheme liabilities:					
Amount	**£(0.3)m**	£(0.0)m	£1.9m	£(0.0)m	£(0.0)m
Percentage of year-end present value of scheme liabilities	**0.6%**	0.0%	(4.4)%	0.0%	0.0%
Total amount recognised in statement of comprehensive income:					
Gain /(loss) before tax	**£2.6m**	(4.4)m	£(3.3)m	£0.6m	£0.4m
Percentage of year-end present value of scheme liabilities	**5.0%**	8.5%	7.5%	1.6%	1.1%

25. Called up share capital

	2021 £m	2020 £m
Authorised, allotted, called-up and fully paid:		
105,000,000 ordinary shares of £1 each	105.0	105.0
	105.0	**105.0**

26. Financial commitments and contingent assets/liabilities

	2021 £m	2020 £m
Loan Commitments		
Expiring in less than one year	96.4	37.3
Expiring in more than one year	-	19.4
	96.4	**56.7**

Capital commitments
The Bank had contracted capital commitments amounting to £nil at 30 September 2021 (2020: £nil).

27. Financial instruments

a) Categories of financial assets and liabilities

Financial assets and liabilities are measured on an on-going basis either at fair value or at amortised cost.

The accounting policies note describes how the classes of financial instruments are measured and how income and expenses including fair value gains and losses, are recognised. The following tables analyse the financial assets and liabilities in the Balance Sheet by the class of financial instrument to which they are assigned and by the measurement basis and include both non-financial assets and liabilities in order to reconcile the disclosures to Balance Sheet totals.

As at 30 September 2021	At amortised cost £m	FVTPL £m	Total £m
Assets			
Cash and balances held at central banks	412.2	-	412.2
Government bonds	29.8	-	29.8
Debt securities	42.3	-	42.3
Loans and advances to credit institutions	45.9	-	45.9
Loans and advances to customers	982.8	78.7	1,061.5
Other assets	6.6	-	6.6
Total financial assets	**1,519.6**	**78.7**	**1,598.3**
Total non-financial assets	115.1	-	115.1
Total assets	**1,634.7**	**78.7**	**1,713.4**
Liabilities			
Deposit from banks	145.0	-	145.0
Deposit from customers	1,381.0	-	1,381.0
Derivative financial instruments	-	14.7	14.7
Other liabilities	9.9	-	9.9
Total financial liabilities	**1,535.9**	**14.7**	**1,550.6**
Total non-financial liabilities	14.2	-	14.2
Share capital and other reserves	148.6	-	148.6
Total reserves and liabilities	**1,698.7**	**14.7**	**1,713.4**

27. Financial instruments (continued)

a) Categories of financial assets and liabilities (continued)

As at 30 September 2020	At amortised cost £m	FVTPL £m	Total £m
Assets			
Cash and balances held at central banks	147.9	-	147.9
Government bonds	48.6	-	48.6
Debt securities	50.7	-	50.7
Loans and advances to credit institutions	105.2	-	105.2
Loans and advances to customers	704.0	226.8	930.8
Other assets	9.9	-	9.9
Total financial assets	**1,066.3**	**226.8**	**1,293.1**
Total non-financial assets			116.1
Total assets			**1,409.2**
Liabilities			
Deposit from banks	87.5	-	87.5
Deposit from customers	1,071.4	-	1,071.4
Derivative financial instruments	-	82.0	82.0
Other liabilities	6.3	-	6.3
Total financial liabilities	**1,165.2**	**82.0**	**1,247.2**
Total non-financial liabilities			21.0
Share capital and other reserves			141.0
Total reserves and liabilities			**1,409.2**

27. Financial instruments (continued)

b) Fair value estimation

The table below summarises the fair value of the Bank's financial assets and liabilities. The different levels have been defined as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities.
- Level 2: Valuation techniques for which all significant inputs are based on observable market data.
- Level 3: Valuation techniques for which significant inputs are not based on observable market data.

Where applicable, the Bank measures the fair value of an instrument using the quoted price in an active market for that instrument. A market is regarded as active if transactions take place with sufficient frequency and volume to provide pricing information on an on-going basis. For all other financial instruments, the Bank determines fair value using other valuation techniques.

The fair value of financial assets and liabilities carried at amortised cost approximate to their carrying value on the Balance Sheet.

The following table presents the Bank's financial assets and liabilities that are measured at fair value on the face of the Balance Sheet and the disaggregation by fair value hierarchy and product type:

As at 30 September 2021	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value through profit or loss				
Loans and advances to customers	-	-	78.7	78.7
Total financial assets at FVTPL	**-**	**-**	**78.7**	**78.7**
Financial liabilities at fair value through profit or loss				
Derivative financial instruments	-	14.7	-	14.7
Total financial liabilities at FVTPL	**-**	**14.7**	**-**	**14.7**

As at 30 September 2020	Level 1 £m	Level 2 £m	Level 3 £m	Total £m
Financial assets at fair value through profit or loss				
Loans and advances to customers	-	-	226.8	226.8
Total financial assets at FVTPL	**-**	**-**	**226.8**	**226.8**
Financial liabilities at fair value through profit or loss				
Derivative financial instruments	-	82.0	-	82.0
Total financial liabilities at FVTPL	**-**	**82.0**	**-**	**82.0**

c) Level 1 and 2 assets and liabilities measured at fair value

Derivative financial instruments: Derivative products (interest rate swaps) use a valuation technique with observable market inputs, their fair value is based on counterparty valuations. Those valuations are tested for reasonableness by discounting estimated future cash flows based on the terms and maturity of each contract and using market interest rates for a similar instrument at the measurement date.

The fair value of financial instruments that are not traded in an active market (for example, over the counter derivatives) is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in Level 2.

Transfers
There were no transfers between Levels 1 and 2 during the year.

27. Financial instruments (continued)

d) Level 3 assets and liabilities measured at fair value

Loans and advances to customers – equity release and retirement mortgages:
Loans and advances to customers include £78.7m (2020: £226.8m) of assets which have been classed as FVTPL and include equity release and retirement mortgages.

	Fair Value		Book Value	
	2021	2020	2021	2020
	£m	£m	£m	£m
Loans and advances (equity release and retirement mortgages) – classified as FVTPL	78.7	226.8	77.7	178.3
	78.7	**226.8**	**77.7**	**178.3**

Reconciliation of the opening and closing recorded amount of Level 3 loans secured by equity release and retirement mortgages:

	2021	2020
	£m	£m
At start of period	226.8	248.3
Disposal of equity release portfolio to a third party	(112.1)	-
Loss on disposal	(5.5)	-
Fair value losses in the Income Statement	(3.9)	(3.7)
Loans advanced	0.6	2.2
Redemptions	(27.2)	(20.0)
At end of financial period	**78.7**	**226.8**

The 15-year point on the risk-free yield curve plus illiquidity spread used for discounting the future retirement mortgage cash flows has increased from 0.39% plus a 2.31% illiquidity spread to 1.01% plus a 2.44% illiquidity spread.

27. Financial instruments (continued)

d) Level 3 assets and liabilities measured at fair value (continued)

Equity release and retirement mortgages - principal assumptions
Principal assumptions in the calculation of equity release and retirement mortgages include:

Mortality or entry into long term care
This is based on the expected death or entry into long term care of the customer or the last remaining customer for a joint contract. Mortality assumptions have been derived by reference to PCMA00/PCFA00. This table is adjusted from 2000 to 31 December 2018 for mortality improvements based on the CMI 2017 mortality projection model. The table is further adjusted from 31 December 2018 to 31 December 2020 using the CMI 2018 mortality projection model, and mortality improvements from 31 December 2020 onwards are based on the CMI 2018 mortality projections model. Finally, the mortality tables are adjusted to reflect recent mortality experience by multiplying the mortality rates by a percentage factor. Given that the CMI 2018, 2019 and 2020 mortality projection models produce similar life expectancies, the mortality improvement assumption for the 2021 year-end is unchanged; in particular, in light of the high level of uncertainty associated with the impact of COVID-19 on mortality improvements over the medium to long-term we have assumed no impact of COVID-19 on future mortality improvements.

Lapses
The fair value for retirement mortgages is materially insensitive to the choice of early redemption assumption. Due to limited market information, this assumption is derived from the Bank's own experience on this product.

Expenses
Assumptions for future policy expense levels are based on the Bank's recent experience analyses. Expenses are modelled as an amount per policy per annum that incorporates an annual inflation rate allowance of 4.58% p.a. as at 30 September 2021 (2020: 4.09% p.a.). This rate is equal to the market implied rate of RPI inflation (appropriate for the average duration of the retirement mortgage portfolio) plus an allowance for expenses increasing faster than the market expectation of prices.

Interest rate
The interest rate used to value the retirement mortgage portfolio comprises two parts: a risk-free yield curve plus a spread referred to as the illiquidity spread.

The risk-free yield curve is based on the PRA's Solvency II curve methodology, which uses SONIA swap rates. An internal tool developed by Milliman is used to derive a proxy for the PRA curve; this is then validated against the actual PRA curve when it is published.

The average discount rate for the portfolio (assumed to be the 15-year point on the yield curve based on the expected average duration) at 30 September 2021 was 3.45% p.a. - including an illiquidity spread of 2.44% (2020: 3.39% p.a.).

No-negative equity guarantee
The fair value of loans secured by retirement mortgages takes into account an explicit provision in respect of the no-negative equity guarantee, calculated using a variant of the Black Scholes option pricing model. The key assumptions used to derive the value of the no-negative equity guarantee include property growth, volatility and credit risk.

The current property price is based on the last survey valuation adjusted by the Nationwide Regional House Price Index with an annual underperformance assumption. The future property price is based on a Future HPI assumption with an annual underperformance assumption.

The property growth (net of underperformance) and volatility assumed at 30 September 2021 is 3.71% (2020: 3.09%) and 15.0% (2020: 13.0%) respectively. The value of the no-negative equity guarantee as at 30 September 2021 is £0.1m.

27. Financial instruments (continued)

Sensitivity analysis

Changes to unobservable inputs used in the valuation technique could give rise to significant changes in the fair value of the assets. The Bank has estimated the net decrease in profit before tax for the period arising from changes to these inputs as follows:

	Interest rates +100 BP £m	Maintenance expenses +10% £m	Property inflation -100bps £m	Property prices -10% £m	Lapses +10% £m	Delay in mortality +10% £m
30 September 2021	**(0.5)**	**(0.4)**	**(0.1)**	**(0.1)**	**(0.0)**	**(0.0)**
30 September 2020	(13.4)	(0.4)	(3.2)	(3.9)	(3.9)	(1.3)

The decrease in the sensitivity output is as a result of the Bank disposing of the majority of its equity release mortgage portfolio during the year. The sensitivity factors are applied via actuarial models. The analysis has been prepared for a change in each variable with other assumptions remaining constant. In reality, such an occurrence is unlikely due to correlation between the assumptions and other factors. It should also be noted that these sensitivities are non-linear and larger or smaller impacts cannot be interpolated or extrapolated from these results. These sensitivities are chosen as they are all key components of the fair value calculation. The sensitivity factors take into consideration that the Bank's assets and liabilities are actively managed and may vary at the time that any actual market movement occurs. In addition, swaps taken out will mitigate some of these sensitivities to movements in rates disclosed above.

27. Financial instruments (continued)

e) Maturity profile of financial assets and liabilities

The table below analyses the carrying value of financial assets and liabilities into relevant maturity grouping based on the remaining period to the contractual maturity date. In practice, customer deposits will be repaid later than on the earliest date on which repayment can be required. Likewise, in practice, customer assets may be repaid ahead of their contractual maturity. As such, the Bank uses past performance of each asset and liability class along with management judgement to forecast likely cash flow requirements.

As at 30 September 2021	Not more than three months £m	More than three months but not more than six months £m	More than six months but not more than one year £m	More than one year but not more than five years £m	More than five years £m	Total £m
Assets						
Cash and balances held at central banks	412.2	-	-	-	-	412.2
Government bonds	-	-	-	-	29.8	29.8
Debt securities	6.1	0.5	-	34.7	1.0	42.3
Loans and advances to credit institutions	45.9	-	-	-	-	45.9
Loans and advances to customers	89.2	30.8	44.0	229.6	667.9	1,061.5
Other assets	6.6	-	-	-	-	6.6
Total financial assets	**560.0**	**31.3**	**44.0**	**264.3**	**698.7**	**1,598.3**
Liabilities						
Deposit from banks	-	-	-	145.0	-	145.0
Deposit from customers	460.9	77.7	270.6	568.7	3.1	1,381.0
Derivative financial instruments	(0.1)	0.1	0.3	1.4	13.0	14.7
Other liabilities	9.9	-	-	-	-	9.9
Total financial liabilities	**470.7**	**77.8**	**270.9**	**715.1**	**16.1**	**1,550.6**
Loan commitments	**93.0**	**0.1**	**3.3**	**-**	**-**	**96.4**

27. Financial instruments (continued)

e) Maturity profile of financial assets and liabilities (continued)

As at 30 September 2020	Not more than three months £m	More than three months but not more than six months £m	More than six months but not more than one year £m	More than one year but not more than five years £m	More than five years £m	Total £m
Assets						
Cash and balances held at central banks	147.9	-	-	-	-	147.9
Government bonds	12.1	6.0	-	-	30.5	48.6
Debt securities	1.1	3.0	-	41.4	5.2	50.7
Loans and advances to credit institutions	105.2	-	-	-	-	105.2
Loans and advances to customers	77.6	39.2	36.1	277.0	500.9	930.8
Other assets	9.9	-	-	-	-	9.9
Total financial assets	**353.8**	**48.2**	**36.1**	**318.4**	**536.6**	**1,293.1**
Liabilities						
Deposit from banks	2.5	-	-	85.0	-	87.5
Deposit from customers	318.2	101.0	325.6	318.1	8.5	1,071.4
Derivative financial instruments	(0.3)	(0.1)	0.4	12.7	69.3	82.0
Other liabilities	6.3	-	-	-	-	6.3
Total financial liabilities	**326.7**	**100.9**	**326.0**	**415.8**	**77.8**	**1,247.2**
Loan commitments liabilities	**34.9**	**0.5**	**7.4**	**13.5**	**0.4**	**56.7**

27. Financial instruments (continued)

f) Maturity profile of financial liabilities-contractual undiscounted cash flows

The table below analyses the Bank's non-derivative financial liabilities and net-settled derivative financial liabilities into relevant maturity groupings based on the period to maturity at the Balance Sheet. Derivative financial liabilities are included in the analysis if their contractual maturities are essential for an understanding of the timing of the cash flows. The amounts disclosed in the table are the contractual undiscounted cashflows.

As at 30 September 2021	Book value	Not more than three months	More than three months but not more than six months	More than six months but not more than one year	More than one year but not more than five years	More than five years	Total
	£m	£m	£m	£m	£m	£m	£m
Financial liabilities							
Deposit from banks	145.0	-	-	-	145.5	-	145.5
Deposit from customers	1,381.0	461.2	78.0	272.8	588.6	3.3	1,403.9
Derivative financial instruments	14.7	0.2	1.0	1.9	7.8	18.5	29.4
Other liabilities	9.9	9.9	-	-	-	-	9.9
Total financial liabilities	**1,550.6**	**471.3**	**79.0**	**274.7**	**741.9**	**21.8**	**1,588.7**

As at 30 September 2020	Book value	Not more than three months	More than three months but not more than six months	More than six months but not more than one year	More than one year but not more than five years	More than five years	Total
	£m	£m	£m	£m	£m	£m	£m
Financial liabilities							
Deposit from banks	87.5	2.5	-	-	85.3	-	87.8
Deposit from customers	1,071.4	318.8	101.6	329.0	331.6	9.2	1,090.2
Derivative financial instruments	82.0	0.1	1.9	5.1	43.8	110.4	161.3
Other liabilities	6.3	6.3	-	-	-	-	6.3
Total financial liabilities	**1,247.2**	**327.7**	**103.5**	**334.1**	**460.7**	**119.6**	**1,345.6**

The above disclosures do not directly align to those presented for the Balance Sheet as they include interest relating to future periods.

The contractual undiscounted cash flows related to derivative financial instruments used for risk management purposes are the net amounts for derivatives that are settled on a net basis.

g) Foreign currencies

The Bank holds no financial assets or liabilities denominated in foreign currencies.

28. Financial risk management objectives and policies

Risk management

The risk management approach encompasses the requirements for identifying, assessing, managing, monitoring and reporting on risk.

The evaluation of the various risks and the setting of policy is carried out through the Bank's Executive Risk Committee which reports to the Risk and Conduct Committee, which ensures adherence to the Bank's Risk Management Policy and Framework.

Risk management objectives

Risk is inherent in all aspects of the Bank's business. The Risk Management Framework is in place to ensure that all material risks faced by the Bank have been identified and measured, and that appropriate controls are in place to ensure that each risk is mitigated to an acceptable degree.

In the normal course of its business, the Bank is exposed to credit risk, liquidity risk, house price risk, interest rate risk, conduct risk and operational risk. These are discussed in more detail in sections a) to f) below.

(a) Credit risk

Credit risk is the risk that borrowers or a counterparty will be unable or unwilling to meet a commitment that they have entered into with the Bank.

The maximum credit risk as at 30 September is the carrying value recognised on the Balance Sheet as disclosed in the table in note 27(a), along with the loan commitments as disclosed in the table in note 27(e).

Credit risk within the commercial lending portfolio is defined as a borrower's inability to repay or service their debt obligations. The primary drivers of credit risk in the Bank's case are property price risk and tenant risk.

The primary driver of credit risk within equity release mortgages and reversionary interests in property is a fall in house prices, which would cause credit losses should house prices fall sufficiently in real terms at the date of redemption.

The primary driver of credit risk within the treasury assets portfolio, which comprises deposits with other banks, government bonds and debt securities is counterparty default, meaning a counterparty can no longer repay its obligations. Only instruments issued by counterparties with a minimum rating of BBB- at the point of purchase are held. The Bank intends to hold its treasury assets to maturity and is therefore not directly affected by market risk.

For both commercial lending and residential mortgages, the Bank takes security in the form of a legal charge over the property against which loans are advanced. The Bank's low risk approach to new business lending is reflected in the loan to value profile of the commercial property and residential property books.

The Bank manages its credit risk through its Retail Credit Committee, Commercial Credit Committee and Assets and Liabilities Committee. Regular credit exposure reports are produced which include information on credit and property underwriting, large exposures, asset concentration and levels of bad debt provisioning.

Credit risk in relation to loans and advances to customers, analysed between residential lending credit risk, commercial lending credit risk and credit risk in relation to treasury financial instruments is described in the relevant sections below.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

Expected Credit Loss Provisioning

Expected credit losses are the discounted product of the Probability of Default (PD), Exposure at Default (EAD), and Loss Given Default (LGD), defined as follows:

- PD is the likelihood of a borrower defaulting on its financial obligation either in the next 12-months or over the remaining lifetime of the obligation.

The calculation of PD is specific to each portfolio as set out below:

Portfolio	Methodology for determining the PD
Residential mortgages	Calculated at an individual account level using the customer's credit score. The PD is derived from UK mortgage account performance data and overlaid with economic forecast assumptions to obtain a forward-looking PD.
Commercial and Portfolio Buy-to-Let	Calculated by making an assessment at an individual account level using a scorecard approach to determine the credit rating of the individual exposure which is linked to historical default rates of comparable entities. A credit cycle overlay model of a credit rating agency is used to calculate the forward-looking PD. The economic assumptions used within this model are obtained from multiple external sources.
Debt securities and government bonds	Calculated at an individual security level using the external credit agency's rating of the security which is linked to the historical default rates of comparable securities.

28. Financial risk management objectives and policies (continued)

Key Economic Scenario Assumptions
The key economic assumptions used to determine the forward-looking PD are as follows:

Portfolio	Y1 %	Y2 %	Y3 %	Y4 %	Y5 %
UK GDP Growth					
Upside	3.8	2.2	1.7	2.0	2.0
Baseline	3.7	1.8	1.3	1.6	1.6
Downside	2.9	1.4	1.0	1.3	1.4
Scenario weighted forecasts	3.4	1.7	1.3	1.6	1.6
UK Unemployment Rate					
Upside	3.9	3.5	3.3	3.3	3.3
Baseline	4.8	4.3	4.1	4.1	4.0
Downside	5.3	4.9	4.8	4.8	4.9
Scenario weighted forecasts	4.8	4.4	4.2	4.2	4.2
% Change in S&P 500 Index[1]	28.1				
% Change in Energy Index	36.2	6.1	1.3	1.4	1.4
% Change in Non-Energy Index	18.1	(2.6)	0.8	0.8	0.8
% Change in Proportion of Downgrades[1]	104.5				

1 These are the historical annual changes and therefore these are only input for Y1 and then updated annually.

The PD models produce an estimate of the point-in-time PD reflecting the current and expected position in the current credit cycle. The models are designed to produce ECL estimates under three distinct scenarios, reflecting expectations of general economic conditions.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

The scenario weightings and the three distinct scenarios used to reflect the expectations of the wider economy that feed into the PD models are:

Scenario	Scenario assumptions	Weighting
Upside	• The key components of the Upside scenario are a quicker global recovery than expected and higher consumer confidence resulting in higher spending.	20.0%
Central	• The key components of the Central scenario are a continued recovery from the COVID-19 pandemic in the next 12 months with a modest growth in GDP thereafter of between 1 and 2%. • The unemployment rate is assumed to peak in Q4 of this year at 5.7% as a result of the removal of the furlough scheme with a gradual reduction in unemployment rates to around 4% in the third year of the forecast. • The anticipated rise in inflation to 4% in early 2022 to be temporary and will reduce as the supply side disruption dissipates.	40.0%
Downside	• The key component of the Downside scenario is the emergence of a new COVID-19 strain and the reintroduction of restrictive measures, prolonged high inflation and continued material and labour shortages.	40.0%

- EAD is based on the amounts the Bank expects to be owed at the time of default.

There are no significant judgements in determining the exposure at default.

- LGD represents the Bank's expectation of the extent of loss on defaulted exposures.

The calculation of LGD is specific to each loan portfolio as set out below:

Portfolio	Methodology for determining the LGD
Residential mortgages	Calculated by using the Black Scholes model to reflect that the portfolio is secured against the underlying property as this will calculate the theoretical value of the total loss, should all policies default.
Commercial and Portfolio Buy-to-Let	Calculated by using an external credit rating agency's ECL model which provides an unbiased estimate of the LGD by blending different probabilities of the economic states occurring (positive, neutral and negative).
Debt securities and government bonds	Calculated on an individual security level using a credit rating agency's published average nominal recovery rate.

A sensitivity analysis has been performed to review the worst-case scenario and the impact on the LGD.

28. Financial risk management objectives and policies (continued)

Credit risk: Residential exposures

The Bank's exposure to credit risk relating to loans and advances to residential customers can be broken down by security as follows:

	2021	
	£m	%
Fully secured by a first charge on residential property	756.7	100.0
	756.7	**100.0**
Fair value adjustments	1.0	
	757.7	

	2020	
	£m	%
Fully secured by a first charge on residential property	534.5	100.0
	534.5	**100.0**
Fair value adjustments	39.3	
	573.8	

The cumulative change in fair values due to credit risk amounts to losses of £0.1m (2020: £7.9m), and the change in the year is a gain of £2.1m (2020: loss of £0.7m).

Residential: risk concentrations
Loan to Value ('LTV') is one of the main factors used to determine the credit quality of loans secured on residential property along with credit scores. All residential loans and receivables have an LTV of less than 75% when advanced.

The Bank provides loans secured on residential property across England, Northern Ireland, Scotland and Wales.

Residential: performance
The gross exposure on loans and advances to residential customers held at amortised cost and its exposure to credit risk in line with the internal modelling of the Bank for the period ending 30 September 2021 is disclosed below:

Stage	Description	Gross Loan Balance	ECL provision
		£m	£m
Stage 1	Satisfactory	654.3	(0.1)
Stage 2	Watchlist	21.4	(0.0)
Stage 3	Default	0.8	(0.0)
		676.5	
Plus: Loan fee deferral		2.6	
Provisions for impairment		(0.1)	
Total		**679.0**	

A deterioration in a customer's credit score since inception of greater than or equal to 160 points results in a loan being moved to Stage 2. Any loan that is 90-days past due is classified as being in default and therefore is allocated to Stage 3.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

The gross exposure on loans and advances to residential customers held at amortised cost and its exposure to credit risk in line with the internal modelling of the Bank for the period ending 30 September 2020 is disclosed below:

Stage	Description	Gross Loan Balance £m	ECL provision £m
Stage 1	Satisfactory	340.4	(0.1)
Stage 2	Watchlist	4.6	(0.0)
Stage 3	Default	0.6	(0.0)
		345.6	
Plus: Loan fee deferral		1.5	
Provisions for impairment		(0.1)	
Total		**347.0**	

The movement between stages based on the gross exposure on loans disclosed below:

Stage	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
At 30 September 2020	340.4	4.6	0.6	345.6
Advances	362.3	-	-	362.3
Stage transfers	(33.0)	32.8	0.2	-
Repayment and settlement	(15.4)	(16.0)	-	(31.4)
At 30 September 2021	**654.3**	**21.4**	**0.8**	**676.5**

Arrears
Performance risk is measured by those accounts in arrears. The total balances in arrears at 30 September 2021 amounted to £1.5m (2020: £1.4m).

Past due but not impaired
As at 30 September 2021 there were no residential exposures that were past due but not impaired (2020: £nil).

Forbearance
There have been no instances of forbearance arising during the year.

Payment holidays
As a result of COVID-19, the Bank granted payment holiday arrangements to a total of 167 Residential customers. All of these customers have resumed full payment.

Sensitivity
A 100% weighting for a negative scenario produces an additional ECL provision for Stage 1, 2 and 3 of £0.1m.

28. Financial risk management objectives and policies (continued)

Credit risk: Commercial lending

Commercial: analysis of risk concentration

Loans secured on commercial property are as follows:

	2021		2020	
	Loan Balance £m	Collateral Held £m	Loan Balance £m	Collateral Held £m
Commercial mortgage	30.2	46.9	30.3	47.8
Development finance	19.1	26.4	34.0	54.8
Investment loans	176.7	292.6	217.9	373.4
Renewable energy	16.3	-	17.7	0.3
	242.3	**365.9**	**299.9**	**476.3**
Less: Loan fee deferral	(1.1)	-	(2.0)	-
Provisions for impairment	(7.3)	-	(7.4)	-
	233.9	**365.9**	**290.5**	**476.3**

At inception, commercial property loans are fully secured against the value of the related properties.

The Bank provides loans secured on property across England, Scotland and Wales. An analysis of commercial property and renewable energy sector loans by geographical location of the underlying asset is provided below:

	2021		2020	
	£m	%	£m	%
Wales	44.0	18.2	59.3	19.8
London – England	99.5	41.1	116.6	38.8
South East & East of England	9.7	4.0	12.6	4.2
Midlands – England	26.4	10.9	27.3	9.1
South West of England	47.1	19.4	44.2	14.8
North West & North East of England	7.5	3.1	29.4	9.8
Scotland	8.1	3.3	10.5	3.5
	242.3	**100.0**	**299.9**	**100.0**

The average LTV in respect of commercial loans is estimated to be 63.7% (2020: 60.3%). LTV analysis has been undertaken by using a combination of external valuations and internal and external desktop reviews which consider the type and quality of security, lease term/tenant as well as geographical location.

£10.6m (2020: £10.2m) of exposures have an LTV of greater than 100%. Of these, £7.3m (2020: £10.2m) are already classified as in default.

The largest exposure to one counterparty is £15.2m (2020: £15.2m) or 6.3% (2020: 5.1%) of gross balances.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

Commercial: lending performance

Procedures are in place which grade borrowers in line with the perceived severity of the risk and are designed to identify cases of potential cause for concern to facilitate early risk mitigation or forbearance activity where appropriate. Using this risk grading system, the gross balance of the commercial loan portfolio is classified as follows:

	2021		2020	
	£m	%	£m	%
Stage 1	159.0	65.6	235.7	78.6
Stage 2 – significant increase in credit risk	66.3	27.4	49.5	16.5
Stage 3 – default	17.0	7.0	14.7	4.9
	242.3	**100.0**	**299.9**	**100.0**

The movement between stages based on the gross exposure on loans disclosed below:

Stage	Stage 1 £m	Stage 2 £m	Stage 3 £m	Total £m
At 30 September 2020	235.7	49.5	14.7	299.9
Advances	24.0	-	-	24.0
Stage transfers	(33.2)	23.5	9.7	-
Repayment and settlement	(67.5)	(6.7)	(7.4)	(81.6)
At 30 September 2021	**159.0**	**66.3**	**17.0**	**242.3**

28. Financial risk management objectives and policies (continued)

Exposure by credit rating
The gross exposure on commercial loans and their exposure to credit risk in line with internal risk grades and the corresponding external credit rating agency's credit risk rating at 30 September 2021 is disclosed below:

Risk grade	Description	Stage	S&P Rating	Gross Loan Balance £m	ECL Provision £m
1	Negligible risk	Stage 1	AAA to A-	-	-
2.1	Minimal risk	Stage 1 or 2	BBB+ to BBB-	-	-
2.2	Low risk	Stage 1 or 2	BB+ to BB	25.4	-
3.1	Fair risk	Stage 1 or 2	BB to BB-	44.8	0.6
3.2	Moderate risk	Stage 1 or 2	B+ to B-	71.2	0.4
4.1	Watch	Stage 1 or 2	B- to CCC	54.4	0.6
4.2	Enhanced watch	Stage 1 or 2	CCC	21.6	0.7
5	Substandard	Stage 2	CCC to CCC-	7.9	-
6	Default	Stage 3	CCC-	9.7	-
7	Loss	Stage 3	CCC-	7.3	5.0
Total				**242.3**	**7.3**

The gross exposure on commercial loans and their exposure to credit risk in line with internal risk grades and the corresponding external credit rating agencies credit risk rating at 30 September 2020 is disclosed below:

Risk grade	Description	Stage	S&P Rating	Gross Loan Balance £m	ECL Provision £m
1	Negligible risk	Stage 1	AAA to A-	0.7	-
2.1	Minimal risk	Stage 1 or 2	BBB+ to BBB-	-	-
2.2	Low risk	Stage 1 or 2	BB+ to BB	27.7	-
3.1	Fair risk	Stage 1 or 2	BB to BB-	46.9	0.1
3.2	Moderate risk	Stage 1 or 2	B+ to B-	116.7	0.3
4.1	Watch	Stage 1 or 2	B- to CCC	55.9	1.1
4.2	Enhanced watch	Stage 1 or 2	CCC	28.3	1.0
5	Substandard	Stage 2	CCC to CCC-	9.0	0.3
6	Default	Stage 3	CCC-	9.7	1.5
7	Loss	Stage 3	CCC-	5.0	3.1
Total				**299.9**	**7.4**

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

Arrears
As at 30 September 2021 there were £3.0m of commercial loans in arrears (2020: £4.1m).

Past due but not impaired
As at 30 September 2021 there was £nil (2020: £nil) commercial loan balances that were past due but not impaired.

Forbearance
There has been one instance of forbearance arising during the year £6.6m (2020: £nil).

Payment holidays
As a result of COVID-19, the Bank granted payment concessions of up to 6 months through to March 2021 on 52 loans. Full payments have resumed on 50 of these loans.

In respect of the concessions, there are 27 loans where the deferred amounts arising from payment concessions have been repaid in full or capitalised by agreement; a further 21 loans where a repayment programme for the deferred amounts has been agreed.

The 2 loans where full payments have not resumed, and where agreement has not been reached to repay the payment concessions granted, relate to 1 customer. This client is in default and has been allocated to Stage 3.

Sensitivity
A 100% weighting for a Negative scenario produces an additional ECL provision for Stage 1 and Stage 2 of £0.9m.

Credit risk: Portfolio Buy-to-Let ('PBTL')

PBTL: analysis of risk concentration
Loans secured on PBTL property are as follows:

	2021		2020	
	Loan Balance £m	Collateral Held £m	Loan Balance £m	Collateral Held £m
PBTL lending	71.5	106.9	63.7	92.6
	71.5	**106.9**	**63.7**	**92.6**

On inception, PBTL property loans are fully secured against the value of the related properties.

The Bank's PBTL loan portfolio comprises the following:

	2021		2020	
	£m	%	£m	%
Loans secured on PBTL property	71.5	100.0	63.7	100.0
	71.5	**100.0**	**63.7**	**100.0**
Less: Loan fee deferral	(0.1)		(0.2)	
Provisions for impairment	(0.9)		(0.4)	
	70.5		**63.1**	

28. Financial risk management objectives and policies (continued)

The Bank provides loans secured on property across England, Scotland and Wales. An analysis of PBTL property loans by geographical location is provided below:

	2021		2020	
	£m	%	£m	%
Wales	3.0	4.2	1.9	3.0
London – England	56.4	78.8	46.1	72.2
South East & East of England	2.2	3.1	7.4	11.7
Midlands – England	3.8	5.3	4.1	6.5
North West - England	1.3	2.0	-	-
South West of England	4.8	6.6	4.2	6.6
	71.5	**100.0**	**63.7**	**100.0**

The average LTV in respect of PBTL loans is 64.2% (2020:68.6%). LTV analysis has been undertaken by using a combination of external valuations and internal and external desktop reviews which consider the type and quality of security, lease term/ tenant as well as geographical location. No exposures have an LTV of greater than 100%.

The largest exposure to one counterparty is £11.4m (2020:£11.4m) or 16% (2020:17.9%) of gross balances.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

PBTL: lending performance

Procedures are in place which grade borrowers in line with the perceived severity of the risk and are designed to identify cases of potential cause for concern to facilitate early risk mitigation or forbearance activity where appropriate. Using this risk grading system, the gross value of the PBTL portfolio is classified as follows:

	2021		2020	
	£m	%	£m	%
Stage 1	55.9	78.2	63.7	100.0
Stage 2 – significant increase in credit risk	13.4	18.7	-	-
Stage 3 – default	2.2	3.1	-	-
	71.5	**100.0**	**63.7**	**100.0**

The movement between stages based on the gross exposure on loans disclosed below:

Stage	Stage 1	Stage 2	Stage 3	Total
	£m	£m	£m	£m
At 30 September 2020	63.7	-	-	63.7
Stage transfers	(15.6)	13.4	2.2	-
Advances	14.5	-	-	14.5
Repayment and settlement	(6.7)	-	-	(6.7)
At 30 September 2021	**55.9**	**13.4**	**2.2**	**71.5**

28. Financial risk management objectives and policies (continued)

PBTL: lending provisions
Exposure by credit rating
The gross exposure on PBTL financial assets and its exposure to credit risk in line with an external credit rating agency's credit risk rating is disclosed below:

30 September 2021

Risk grade	Description	Stage	Credit Rating	Gross Loan Balance £m	ECL Provision £m
2.2	Low risk	Stage 1	BB+ to BB	7.2	-
3.1	Fair risk	Stage 1 or 2	BB to BB-	10.5	-
3.2	Moderate risk	Stage 1 or 2	B+ to B-	35.9	(0.5)
4.1	Watch	Stage 1 or 2	B- to CCC	15.7	(0.4)
6	Default	Stage 3	CCC-	2.2	-
Total				**71.5**	**(0.9)**

30 September 2020

Risk grade	Description	Stage	Credit Rating	Gross Loan Balance £m	ECL Provision £m
3.1	Fair risk	Stage 1 or 2	BB to BB-	3.1	(0.0)
3.2	Moderate risk	Stage 1 or 2	B+ to B-	60.6	(0.4)
Total				**63.7**	**(0.4)**

Arrears
As at 30 September 2021 there were £2.2m PBTL loans in arrears (2020: £nil).

Past due but not impaired
As at 30 September 2021 there were no PBTL loans that were past due but not impaired (2020: £nil).

Forbearance
There have been no instances of forbearance arising during the year.

Payment holidays
As a result of COVID-19, the Bank granted a payment holiday to four PBTL customers. All of these customers have resumed full payment, one is allocated to Stage 1, two to Stage 2 and one to Stage 3.

Sensitivity
A 100% weighting for a Negative scenario produces an additional ECL provision for Stage 1 and 2 of £0.4m.

28. Financial risk management objectives and policies (continued)

(a) Credit risk (continued)

Credit risk: Treasury assets

Treasury risk comprises exposure to central banks, government bonds, debt securities, credit institutions and financial derivatives. The following table shows the maximum exposure to credit risk excluding collateral:

	2021 £m	2020 £m
Cash and balances held at central banks	412.2	147.9
Government bonds	29.8	48.6
Debt securities	42.3	50.7
Loans and advances to credit institutions	45.9	105.2
	530.2	**352.4**
Provision for impairment	-	-
Total	**530.2**	**352.4**

None of these exposures are past due or impaired.

Credit quality of financial assets that are neither past due nor impaired
The following shows the exposures broken down by credit rating:

	2021 £m	2020 £m
AAA to AA-	530.2	352.4
	530.2	**352.4**

Concentration of credit risk
The geographical exposure is as follows:

	2021 £m	2020 £m
UK	517.1	335.1
Other	13.1	17.3
	530.2	**352.4**

The Treasury function monitors exposure concentrations against a variety of criteria including counterparty limits.

28. Financial risk management objectives and policies (continued)

b) Liquidity risk

Liquidity risk is the risk that the Bank will encounter difficulty in realising assets or otherwise raising funds to meet commitments as they fall due. The Bank manages its liquidity risk through its Assets and Liabilities Committee and monitors its liquidity position on a daily basis and has adopted a policy to ensure that it has adequate resources to enable it to conduct its normal business activities without interruption. The maturity analysis of assets and liabilities is disclosed in note 27 (e) & (f) to the financial statements of the Bank.

The customer deposit base represents a stable source of funding due to the number and range of depositors. Liquidity is further managed through dealings in the money markets.

The Board has approved a Liquidity Risk Management policy that sets out the liquidity requirements with which the Bank must comply. The principal liquidity risk mitigants used by management are:

- A buffer of highly liquid assets (comprising high quality government, covered bonds and supranational bank securities) which can meet cash requirements;
- Cash reserves with the Bank of England;
- Cash resources held at other financial institutions.

c) Interest rate risk

Interest rate risk is the risk that arises when there is an imbalance between the maturity dates of rate-sensitive assets, liabilities and commitments. The Bank manages its interest rate risk through its Assets and Liabilities Committee. The Bank's policy is to maintain interest rate risk at a controlled level within limits set by the Board.

The table in note 27 (d) shows an estimate of the interest rate sensitivity gap as at 30 September 2021. The principal risk management tool to mitigate interest rate risk is the use of derivatives to align the interest rate re-pricing profile of assets and liabilities. All of the derivatives used by the Bank are interest rate swap contracts of varying maturities and start dates.

The Bank's Interest Rate Risk Management policy defines the type of derivative transactions that can be undertaken, which are all actioned by the Bank's Treasury function, and are subject to review and approval at the dealing stage. The Treasurer, who is responsible for treasury matters on a day to day basis, prepares a treasury report for the Board, which includes analysis of interest rate risk exposures.

d) Operational risk

Operational risk is the risk of economic loss from systemic failure, human error and fraud (control failures) or external events, which result in unexpected or indirect loss to the Bank. When controls fail to perform, operational risks can cause damage to reputation, have legal or regulatory implications or can lead to financial loss. The Bank cannot expect to eliminate all operational risks but by initiating a rigorous control framework and by monitoring and responding to potential risks, the Bank is able to manage the risks. Controls include effective segregation of duties, access controls, authorisation and reconciliation procedures, staff education and assessment processes, including the use of internal audit.

The Bank has responded to COVID-19 as it developed, initially through its business continuity processes to ensure the safety of its colleagues and its customers before returning to a more 'business as usual' operation albeit operating remotely. Hodge has responded to and follows government guidance and best practice to maintain our customer service levels and protect our employees.

28. Financial risk management objectives and policies (continued)

e) House price risk

House price risk is the risk that arises when there is an adverse mismatch between actual house prices and those implicit in the costing of the Bank's equity release, retirement mortgages and reversionary interests held at FVTPL such that the ultimate realisation of the property would not yield the expected return to the Bank and could, in certain circumstances, result in a capital loss. The Bank mitigates house price risk by monitoring maximum loan to value at inception of the loan and reversionary interests.

Geographical analysis of equity release and retirement mortgages

The Bank provides loans secured on property across England, Scotland, Northern Ireland and Wales. An analysis of residential property by geographical location is provided below. The Bank disposed of its equity release portfolio in the year:

	2021		2020	
	£m	%	£m	%
Wales	3.3	4.4	9.3	5.2
East Anglia	2.9	3.8	7.4	4.2
East Midlands	3.5	4.7	8.8	5.0
Greater London	5.0	6.6	16.4	9.2
Yorkshire & Humberside	5.5	7.3	14.0	7.9
North West	7.2	9.5	19.1	10.6
Northern Ireland	-	-	8.9	5.0
Scotland	14.4	19.0	19.7	11.0
Outer Metropolitan	5.2	6.9	13.7	7.7
Outer South East	10.6	14.0	20.8	11.6
South West	9.0	11.9	20.2	11.4
West Midlands	5.4	7.1	10.8	6.0
North	3.7	4.8	9.2	5.2
	75.7	**100.0**	**178.3**	**100.0**

28. Financial risk management objectives and policies (continued)

f) Conduct risk

Conduct risk is the risk that the Bank's behaviour results in poor outcomes for customers. The Bank is exposed to this risk by virtue of the markets in which it chooses to operate. The Executive Risk Committee has overall responsibility for implementing and monitoring principles, frameworks, policies and limits. The Committee is responsible for managing risk decisions and monitoring risk levels which it reports to the Risk and Conduct Committee.

The Bank holds a provision of £nil as at 30 September 2021 (2020: £nil).

g) Pension risk

The Bank is exposed to pension risk through its defined benefit scheme. Further information is provided in note 24.

h) Pandemic risk

Pandemic risk is the risk of economic loss from a result of a pandemic. The Executive Risk Committee has overall responsibility for implementing and monitoring risks that a pandemic could cause. The Committee is responsible for managing risk decisions and monitoring risk levels which it reports to the Risk and Conduct Committee.

29. Capital risk management (unaudited)

The Bank conducts an Internal Capital Adequacy Assessment Process ('ICAAP'), at least annually, which is approved by the Board. This is used to assess the Bank's capital adequacy and to determine the level of capital required to support the future development of the business as set out in the strategic plan.

The ICAAP considers all of the Bank's material risks and includes board-approved stress scenarios which are intended, as a minimum, to meet regulatory requirements. The ICAAP is used by the PRA to set the Bank's Total Capital Requirements ('TCR').

The Bank's capital resources requirements are calculated based on the CRD IV CRR regulatory framework as implemented by the PRA, namely:

- Pillar 1-based on a Standardised Approach for credit risk, operational risk and market risk;
- Pillar 2-set by the PRA via the TCR to address those risks not covered under Pillar 1.

The Board is ultimately responsible for capital management and monitors the capital position of the Bank at each board meeting through the receipt of management information which sets out the Bank's current and forecast capital position, based on the methodology adopted within its ICAAP. This means that the Bank will:

i) Maintain a level of capital at least equal to the minimum amount set by the PRA in the TCR, and;

ii) Hold all its capital in the form of Common Equity Tier 1 and Tier 2 capital.

	2021 Unaudited £m	2020 Unaudited £m
Common Equity Tier 1 capital	143.8	136.4
Total risk weighted assets	771.0	693.8
Common Equity Tier 1 capital ratio	**20.2%**	**19.7%**
Total own funds	143.8	136.4
Total risk weighted assets	771.0	693.8
Total capital ratio	**20.2%**	**19.7%**

Capital Requirements Directive
Article 89 of the Capital Requirements Directive IV (CRD IV) requires credit institutions and investment firms in the EU to disclose annually, specifying, by Member State and by third country in which it has an establishment, the following information:

- Name, nature of activities and geographical location: The principal activities of the Bank are noted in the Strategic Report.
- Average number of employees: as disclosed in note 6 to the accounts.
- Annual turnover (Net Interest Income) and profit before tax: as disclosed in the Income Statement.
- Corporation Tax paid: 2021: £nil (2020: £0.4m).
- Public subsidies: The Bank received £nil (2020:£0.3m) under the Coronavirus Job Retention Scheme from the UK government.

All minimum regulatory requirements were met during the year and the prior year.

The Bank's objectives when managing capital are:

- To have sufficient capital to safeguard the Bank's ability to continue as a going concern so that it can continue to provide returns for the Shareholders and benefits for other stakeholders;
- To comply with the Bank's capital requirements set out by the PRA in the UK;

The Bank's capital comprises all components of equity, movements of which are set out in the Statement of Changes in Equity.

30. Related parties

The Bank has applied the exemptions available under FRS 101 in respect of transactions with members of The Carlyle Trust Limited group. The following balances were owed to or from related parties at 30 September 2021 and 30 September 2020:

	2021 £m	2020 £m
Amounts due/(owed) from parent and fellow subsidiaries		
The Carlyle Trust Limited – parent	0.3	3.1
Reimbursement asset due from The Carlyle Trust Limited	-	3.3
Group relief debtor	0.1	2.9
Total	**0.4**	**9.3**
Jane Hodge Foundation – shareholder of The Carlyle Trust Limited	(3.5)	(1.8)
Deposits owed to parent and fellow subsidiaries		
Hodge Developments Beaufort Park Limited	(0.1)	(0.1)
Sterling House Limited	(0.2)	(0.1)
Wingwest (Fountain Lane) Limited	(0.2)	(0.1)
The Carlyle Trust Limited – parent	(128.6)	(1.3)
Carlyle Property Development Limited	(0.7)	-
Hodge Limited	(2.9)	-
Total	**(132.7)**	**(1.6)**

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